Supreme Court, U.S.
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No. 07-995

In The
Supreme Court of the United States

STEVE SANDERS,
individually and as class representative
Petitioner,

v.

EDMUND G. BROWN, in his official capacity as Attorney general of the State of California, PHILIP MORRIS USA, INC., R.J. REYNOLDS TOBACCO CO., BROWN & WILLIAMSON TOBACCO CORP., and LORILLARD TOBACCO CO.,
Respondents.

On Petition for Writ of Certiorari
To the United States Court of Appeals for the Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

This case involves an antitrust challenge to the so-called Master Settlement Agreement ("MSA") between the four major tobacco companies and 46 States, and legislation enacted to implement the agreement. The questions presented are:

1. Whether the Ninth Circuit erred in holding, in conflict with the Second Circuit, that the MSA implementing statutes are not pre-empted by the Sherman Antitrust Act?

2. Whether the Ninth Circuit erred in holding, in conflict with the Second Circuit, that the *Noerr-Pennington* doctrine applies not only to protect petitioning activity, but also to immunize any resulting anticompetitive legislation and conduct undertaken pursuant thereto, regardless whether the legislation fails to qualify for protection from federal pre-emption under the state-action doctrine?

3. Whether the Ninth Circuit erred in holding, in conflict with the Second and Third Circuits, that the *Parker* state-action immunity doctrine applies to the conduct of a state executive officer in entering into a settlement agreement and administering state laws that together are part of an anticompetitive scheme, regardless whether such settlement and laws would satisfy the *Midcal* test for state-action immunity?

PARTIES TO THE PROCEEDINGS BELOW

Petitioner Steve Sanders was the appellant in the Ninth Circuit and the plaintiff in the district court.

Respondent Edmund G. Brown, as Attorney General of the State of California, was substituted as an appellee below when he replaced his predecessor, Bill Lockyer, as Attorney General. Former Attorney General Lockyer was initially an appellee in the Ninth Circuit and was a defendant in the district court.

Respondents Phillip Morris USA, Inc., R.J. Reynolds Tobacco Co., Brown & Williamson Tobacco Corp., and Lorillard Tobacco Co. were each appellees in the Ninth Circuit and were each defendants in the district court. Each defendant, respectively, is ultimately owned by the following publicly held company: Altria Group, Inc., Reynolds American Inc., British American Tobacco, p.l.c., and Loews Corporation.

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PETITION FOR WRIT OF CERTIORARI

Petitioner Steve Sanders respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit.

OPINIONS BELOW

The opinion of the District Court for the Northern District of California is published at 365 F. Supp.2d 1093 and is attached as Appendix B (pages B1-B23). The decision of the Ninth Circuit is published at 504 F.3d 903 and is attached as Appendix A (pages A1-A31).

JURISDICTION

The Ninth Circuit issued its opinion on September 26, 2007. Justice Kennedy granted petitioner an extension of time to file this petition through January 25, 2008. This Court has jurisdiction pursuant to 23 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 1 of the Sherman Act, states that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce * * * is declared to be illegal." 15 U.S.C. § 1.

California's so-called Qualifying Act, also sometimes referred to as the Escrow Statute, provides in relevant part:

> (a) Any tobacco product manufacturer selling cigarettes to consumers within the state, whether directly or through a distributor, retailer or similar intermediary or intermediaries, after the date of enactment of this article shall do one of the following:

(1) Become a participating manufacturer as that term is defined in Section II(jj) of the Master Settlement Agreement and generally perform its financial obligations under the Master Settlement Agreement; or

(2) Place into a qualified escrow fund by April 15 of the year following the year in question the following amounts, as such amounts are adjusted for inflation:

[Setting forth amounts per unit sold beginning at $0.0094241 for 1999 and rising to $0.0188482 for 2007 and thereafter.]

(b) Any tobacco product manufacturer that places funds into escrow pursuant to paragraph (2) of subdivision (a) shall receive the interest or other appreciation on the funds as earned. The funds, other than the interest or other appreciation, shall be released from escrow only under the following circumstances:

(1) To pay a judgment or settlement on any released claim brought against that tobacco product manufacturer by the state or any releasing party located or residing in the state. * * *

(2) To the extent that a tobacco product manufacturer establishes that the amount it was required to place into escrow on account of units sold in this state in a particular year was greater than the Master Settlement Agreement payments * * * that the manufacturer would have been required to make on account of the units sold had it been a participating manufacturer, the excess shall be released from escrow and revert back to that tobacco product manufacturer; or

> (3) To the extent not released from escrow under paragraph (1) or (2) of subdivision (b), funds shall be released from escrow and revert back to the tobacco product manufacturer 25 years after the date on which they were placed into escrow. * * *

CAL. HEALTH & SAFETY CODE § 104557.

California's so-called Contraband Amendment provides, in relevant part:

> (a) Commencing on January 1, 2004, every manufacturer and every importer, as defined in subdivision (b) of Section 22971, shall obtain and maintain a license to engage in the sale of cigarettes. * * *
>
> (b) In order to be eligible for obtaining and maintaining a license under this division, a manufacturer or importer that is a "tobacco product manufacturer" in subdivision (i) of Section 104556 of the Health and Safety Code, shall do all of the following in the manner specified by the board:
>
> (1) Certify to the board that it is a "participating manufacturer" as defined in subsection II(jj) of the "Master Settlement Agreement" (MSA), or is in full compliance with paragraph (2) of subdivision (a) of Section 104557 of the Health and Safety Code [the Escrow Statute]. * * *

CAL. BUS. & PROF. CODE § 22979.

STATEMENT OF THE CASE

This case involves an antitrust challenge to the actions of the four major tobacco companies and the State of California under the so-called Master Settlement Agreement ("MSA") negotiated between the

major tobacco companies and 46 States. The MSA was proposed by the major tobacco companies, known under the MSA as the "Original Participating Manufacturers" or "OPMs," to settle suits brought against them by various state attorneys general. Under the MSA, the OPMs agreed to pay the settling States more than $ 200 billion over the next 25 years and to various restrictions on their conduct. The States, in turn, agreed to drop their suits against the OPMs and not to sue them for tobacco sales in the future. Up to that point, the MSA had few antitrust implications.

As proposed by the OPMs, however, and accepted by the state attorneys general, the MSA in fact included provisions designed not only to ensure that the settling manufacturers would be able to pass the full cost of the settlement on to consumers, but also to insulate the defendants from any competitive disadvantage they might face at the hands of their rivals as a result of having raised prices to pay for the settlement. The agreement thus imposed severe disincentives upon any attempt by the OPMs to increase their market share or to compete on price among themselves. In addition, the agreement sought to prevent other tobacco manufacturers from gaining market share at the OPMs' expense as a result of the expected rise in prices. It encouraged other manufacturers to join the settlement as "Subsequent Participating Manufacturers" or "SPMs" by exempting them from any settlement payment obligations if they kept their market share below certain fixed levels. For those companies that refused to join the settlement, the MSA required the States to enact legislation requiring those "Non Participating Manufacturers" or

"NPMs," to pay into state escrow accounts an amount equivalent to the increase in prices the OPMs anticipated having to impose to pay for the settlement, effectively precluding the NPMs from gaining market share based on the anticipated price increases. *See* App. A4-A6.

The result was an agreement among competitors and with state attorneys general to divide the market for tobacco products among participating manufacturers while promoting lockstep price increases and protecting such participating manufacturers by imposing substantial additional costs on potential competitors who were never sued and did not join the settlement.

As alleged in the Complaint, the scheme has in fact worked as the OPMs intended. Following the adoption of the MSA, the OPMs raised their prices by more than $12.20 per carton between 1998 and 2002, generating increased profits of approximately $20 billion per year; more than double that needed to fund their MSA obligations. App. A7. Such price increases have occurred in lockstep and the OPMs and SPMs have not lost any material amount of market share as a result. *Id.*

1. Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1, declares that "[e]very contract, combination * * *, or conspiracy, in restraint of trade or commerce" is illegal. As between private parties, it is well settled that a "horizontal" contract, combination, or conspiracy among competitors to raise prices, divide markets, restrict output, or otherwise to suppress competition is *per se* illegal. *See United States* v. *Topco Assocs.*, 405 U.S. 596, 608 (1972) ("one of the

classic examples of a *per se* violation of § 1 is an agreement between competitors at the same level of the market structure to allocate territories in order to minimize competition. Such concerted action is usually termed a 'horizontal' restraint * * *"); *NAACP* v. *Board of Regents*, 468 U.S. 85, 100, 107-08 (1984) ("Horizontal price fixing and output limitation are ordinarily condemned as a matter of law under an 'illegal *per se*' approach * * *"; "Restrictions on price and output are the paradigmatic examples of restraints of trade that the Sherman Act was intended to prohibit."). Were the MSA solely an agreement between the tobacco companies themselves, there is no doubt that it would constitute a *per se* violation of the Sherman Act and that tobacco company "executives would long ago have had depressing conversations with their attorneys about the United States Sentencing Guidelines." *Freedom Holdings Inc.* v. *Spitzer*, 357 F.3d 205, 226 (CA2 2004) ("*Freedom Holdings I*").

These general principles are, however, subject to various judicially-developed limitations. First, this Court has held that, in enacting the Sherman Act, Congress did not suggest any purpose "to restrain a state or its officers or agents from activities directed by its legislature." *Parker* v. *Brown*, 317 U.S. 341, 350-51 (1943). Relying on principles of federalism and state sovereignty, this Court declined to attribute to Congress, via the Sherman Act, "an unexpressed purpose to nullify a state's control over its officers and agents." *Id.* at 351. Accordingly, under the so-called *Parker* immunity doctrine, this Court has held that the antitrust laws do not apply to a State acting in its sovereign capacity, either through its legislature or

through its state supreme court exercising legislative authority. *Id.* at 350-51 (applying doctrine to "activities directed by [a State's] legislature"); *Hoover* v. *Ronwin,* 466 U.S. 558, 568 (1984) ("[A] state supreme court, when acting in a legislative capacity, occupies the same position as that of a state legislature. Therefore, a decision of a state supreme court, acting legislatively rather than judicially, is exempt from Sherman Act liability as state action.").

Even state action, however, may nonetheless be subject to the Sherman Act if the State acts as a "participant in a private agreement or combination by others for restraint of trade," or when a state seeks to "give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Parker*, 317 U.S. at 351-52. Similarly, a "hybrid restraint," under which a statute "contemplates a private market decision but provides a nonmarket mechanism for enforcing the decision" requires a different analysis than a purely public regulatory scheme, and its validity under the Sherman Act will typically depend on the degree to which the private decisions are supervised by the State. *Rice* v. *Norman Williams Co.*, 458 U.S. 654, 665-66 (1982) (Stevens, J., concurring in the judgment).

Regarding any subsequent anticompetitive conduct supposedly pursuant to state law, *Parker* state-action immunity only extends to such conduct where the challenged restraint is "'one clearly articulated and affirmatively expressed as state policy' [and] the policy [is] 'actively supervised' by the State itself." *California Retail Liquor Dealers Ass'n.* v. *Midcal Alumi-*

num, Inc., 445 U.S. 97, 105 (1980) (citation omitted). A state program failing the so-called *Midcal* test, and merely enforcing or casting "a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement," *id.* at 106, not only will fail to provide immunity for such conduct, it may itself be enjoined as contrary to the Sherman Act, *id.* at 101-02 (affirming injunction barring state department from enforcing wine pricing statutes).

Second, the Court has held, in light of both the *Parker* state-action doctrine and the First Amendment's right to petition the government, that private entities may not be held liable for "activities [that] comprise[] mere solicitation of governmental action with respect to the passage and enforcement of laws." *Eastern R.R. Presidents Conf.* v. *Noerr Motor Freight, Inc.*, 365 U.S. 127, 138 (1961); *United Mine Workers of America* v. *Pennington*, 381 U.S. 657, 670 (1965) ("Joint efforts to influence public officials do not violate the antitrust laws even though intended to eliminate competition."). The protection for such petitioning in the antitrust context is known as the *Noerr-Pennington* doctrine.

2. On June 9, 2004, plaintiff Steve Sanders, a smoker, filed suit on behalf of himself and as putative class representative of similarly situated smokers, alleging that the MSA, the California implementing statutes, and the tobacco companies' ensuing conduct violated, *inter alia*, federal antitrust laws. Class Action Complaint, June 9, 2004 ("Complaint") [ER 001-

025.][1] The Complaint sought declaratory and injunctive relief against the California Attorney General and the OPMs, and also sought damages and restitution from the OPMs.

As was alleged in the Complaint, in 1997 several States sued the four major tobacco companies, respondents here, to recover costs to the States associated with smoking-related illnesses. In response to those suits, the tobacco defendants together formulated, and thereafter proposed to the state attorneys general, a settlement whereby the companies would pay over $200 billion to the States over the next 25 years and agree to various marketing restrictions.

Agreeing to pay the States billions of dollars gave rise to an obvious problem for the defendants. If they maintained their current prices, the MSA payments would substantially erode (and perhaps eliminate) their profits for the next 25 years. On the other hand, if they raised their prices to pay for the settlement, the price increases would put them at a disadvantage vis-à-vis their competitors. The OPMs solved this problem in three ways.

First, they structured their payment obligations under the MSA in a way that strongly discouraged any of the OPMs from seeking to gain market share at each others' expense. In particular, the OPMs agreed and proposed to allocate payment of the an-

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[1] "ER" refers to the Excerpts of Record in the court of appeals. The complaint also alleged violations of state antitrust and unfair competition laws. Those claims, while not directly relevant to the current petition, were disposed of on grounds dependant on the federal antitrust ruling, and thus would, at least at this stage, follow the fate of the federal issues presented here.

nual settlement amounts according to *future* annual market share rather than according to any measure of past conduct or market share. App. A5; MSA § IX(c)(1).[2] Under such allocation method, any OPM gaining future market share would bear a concomitant increase in MSA payment obligations, and any OPM losing relative market share would be compensated by a decrease in MSA payments. App. A5. The Complaint alleged that such payment adjustments would offset any potential gain in profits from a gain in market share. Complaint ¶ 21 [ER 008-009].

Second, the OPMs encouraged other manufacturers to join the MSA as SPMs, and to forgo attempting to gain market share at the OPMs' expense, by offering an exemption from all MSA payments for SPMs who joined promptly and who kept their market share at or below either their 1998 levels or 125% of their 1997 levels, whichever was higher. App. A4-A5; MSA § IX(i). For sales above that level, SPMs would have to pay a portion of the MSA payment. *Id.*

Third, the OPMs guarded against price competition by manufacturers who declined to join the MSA – "Non-Participating Manufacturers" or "NPMs" – by enlisting the States to impose added costs upon such NPMs that would equal (and in reality exceed) the per-cigarette costs of the settlement payments by the OPMs. *See* App. A5-A7; MSA § IX(d). The MSA does this by threatening to reduce or withhold settlement payments to any State that does not enact a so-called Qualifying Statute designed to eliminate any com-

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[2] The MSA and related documentation is available at online at www.naag.org/backpages/naag/tobacco/msa/.

petitive threat the NPMs, with their lower cost structure, might pose to the participating manufacturers. *Id.* Given the draconian penalty for failure to enact and diligently enforce a qualifying statute, virtually all MSA States, including California, have adopted such a statute.

California's Qualifying Act, also sometimes known as the Escrow Statute, is typical, and provides that any manufacturer not participating in the MSA must pay into escrow an amount per cigarette approximately equal to the per cigarette amount paid by the OPMs under the MSA. App. A7; CAL. HEALTH & SAFETY CODE § 104557. Such amounts are to remain in escrow for 25 years unless used to pay any future liability to the State. Unlike MSA payments, however, the escrow payments are not tax deductible, hence their real cost to NPMs is considerably higher than the cost of MSA payments to the OPMs. Complaint ¶ 27(d) [ER 013]. The differential tax treatment of escrow payments and MSA payments thus not only eliminates any competitive disadvantage from the MSA payments, it actually gives participating manufacturers a competitive cost *advantage* that allows them to increase prices well beyond that needed to fund the MSA and still be protected from price competition by the NPMs.

The Qualifying Act is further enforced by the Contraband Amendment, which requires all companies to obtain a license to sell cigarettes within California, and denies a license to any company that does not either join the MSA or make escrow payments. *See* App. A6-A7; CAL. BUS. & PROF. CODE § 22979.

Through a combination of those three elements – OPM payments based on future market share that deter gains in market share, incentives for SPMs to maintain market share at or below fixed levels, and imposition of added costs on NPMs that precluded price competition even well above price levels necessary to fund the MSA – the OPMs effectively established a horizontal output cartel that eliminated all incentive to increase market share or to compete on price, locking in market share and dividing the market among the OPMs, who together account for over 90% of the national cigarette market, *see* App. A3. The scheme likewise drew in numerous SPMs who, together with the OPMs, raised the total market share represented by MSA participants to 96%. App. B3.

Such a market division scheme also created an irresistible pressure upon each OPM to match any price increases by the others in order to avoid financially counterproductive gains in relative market share and to reap supracompetitive profits in the relatively inelastic cigarette market. For example, under the MSA an OPMs' failure to adopt a price increase initiated by one or more of the other OPMs would lead to the lower-priced OPM gaining market share and hence shouldering a larger percentage of the fixed MSA costs. *See* App. A5. The higher-priced OPMs, by contrast, would lose some market share, but they would both have a higher profit margin on the cigarettes they did sell and would pay less of the MSA payments. If all of the OPMs act together, however, none of them would gain or lose market share, they would all have a higher profit margin, and each

OPMs MSA payments would remain the same but constitute a smaller percentage of revenues. The system as designed thus penalizes gains in market share and rewards the maintenance of existing market shares at higher prices.[3]

In a testament to the anticompetitive effectiveness of the MSA, and as alleged in the Complaint, despite price increases of more than $12.20 per carton of cigarettes, generating more than twice the additional profits needed to fund the MSA, the market shares of participating manufacturers have not materially changed since the MSA was adopted. *See* App. A7.

Based upon the foregoing agreements, statutes, and the subsequent conduct of the OPMs in raising prices in lockstep and beyond that necessary to fund their MSA payments, the Complaint alleges the existence of a market-division, output-restriction and price-fixing cartel facilitated and enforced, though not actively supervised, by the State.

3. In response to the Complaint, the tobacco company defendants and the California Attorney General moved to dismiss, relying primarily on the *Noerr-Pennington* and *Parker* immunity doctrines.

4. On March 28, 2005, the district court granted defendants' motions to dismiss. The court concluded that the MSA, the Qualifying Act, and the Contraband Amendment were all protected by the *Parker* state-action doctrine because the MSA was "a sover-

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[3] The incentives are similar for SPMs, who avoid any MSA payments, and increase their profit margin, by tracking the price increases of the OPMs and keeping their market share below the fixed levels specified by the MSA.

eign act of the state of California" and the implementing statutes were "direct legislative activity." App. B11 (citing *Parker* and *Hoover*). The court rejected plaintiff's argument that it apply the two-part test from *Midcal* to determine whether the State had affirmatively expressed and actively supervised its supposed decision to supplant competition, and further held that the MSA and its related statutes were not a "hybrid restraint" disqualified from *Parker* immunity. App. B9-14. In doing so, the court rejected the contrary holding of the Second Circuit in *Freedom Holdings I,* 357 F.3d at 233, that the MSA and its related statutes were a hybrid restraint that failed the *Midcal* test and were preempted. App. B13-14.

The district court also found that the Qualifying Act and the Contraband Amendment were not facially preempted by federal law because the statutes themselves did not expressly permit violations of the antitrust laws and because, in its view, the alleged effects of the statutes in enforcing an anticompetitive scheme were merely hypothetical or potential. App. B14-B16.

As to both the Attorney General and the tobacco defendants, the court held they were immune under the *Noerr-Pennington* doctrine not only for their conduct in negotiating and seeking approval of the MSA, but also for the *results* of such petitioning and their subsequent conduct under the regime established by the MSA and its related statutes. App. B16-B20.

Finally, the district court also extended *Parker* state-action immunity to the tobacco defendants, refusing to apply the *Midcal* test or to find that the MSA arrangement was a hybrid restraint, and con-

cluding that where "there is direct state action affording immunity, the immunity extends equally to private parties and state actors." App. B21. The court rejected the Third Circuit's conclusion in *A.D. Bedell Wholesale Co.* v. *Philip Morris, Inc.*, 263 F.3d 239 (CA3 2001), *cert. denied*, 534 U.S. 1081 (2002) that the *Midcal* analysis applied to the MSA and prevented state-action immunity from extending to tobacco company conduct *after* implementation of the MSA. App. B22.[4]

5. Plaintiff appealed to the Ninth Circuit.

6. On September 26, 2007, the Ninth Circuit affirmed. App. A1-A31.

a. Before the Ninth Circuit, plaintiff argued that the MSA and its related statutes establish an output and price-fixing cartel that is a *per se* antitrust violation, not merely some hypothetical or potential violation, and were not saved from preemption by this Court's decision in *Rice*.

In *Rice*, this Court held that a state statute is preempted by federal antitrust law "on its face without consideration of particular circumstances," only

> if it mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.

---

[4] Regarding the state-law claims, the court found that the legislative acts of the state cannot violate its own laws. App. B23. It did not discuss whether the MSA or the conduct of the tobacco defendants under the MSA could violate such law, though it granted the motion to dismiss on those claims in any event.

> Such condemnation will follow under § 1 of the Sherman Act when the conduct contemplated by the statute is in all cases a *per se* violation.

458 U.S. at 658 n. 4, 661. Plaintiff argued that the MSA and the statutes established an output cartel that was a *per se* violation of the Sherman Act and hence were preempted.

The Ninth Circuit disagreed. It held that the Escrow and Contraband statutes were not preempted because, in its view, the statutes do not "explicitly allow price fixing, market division, or other *per se* monopolistic behavior," and an NPM still "conceivably could compete on price by charging a 'normal' price and still make a 'normal' profit, even taking the escrow payment into account." App. A13. The court thus concluded that the statutes do not "mandate or authorize conduct that 'in all cases' violates federal antitrust law," and hence were not preempted. *Id.* (quoting *Fisher* v. *City of Berkeley*, 475 U.S. 260, 265 (1986) (quoting *Rice*, 458 U.S. at 661)) (internal quotation marks omitted in opinion below).

In so holding, the court below joined the Sixth Circuit in finding that the law was not preempted, *Trident Int'l Corp.* v. *Kentucky*, 467 F.3d 547, 557-58 (CA6 2006), and expressly rejected the Second Circuit's contrary finding of preemption in *Freedom Holdings I*, 357 F.3d at 222-32.

b. Plaintiff also challenged the application of *Noerr-Pennington* immunity to protect the MSA, its related statutes, or the subsequent conduct of the tobacco companies in using the MSA regime to operate a cartel. As described by one of the leading treatises on antitrust law, "*Noerr* protects the petitioning proc-

ess from antitrust liability, but it does not protect all the results of such petitioning." 1 Phillip E. Areeda & Herbert Hovenkamp, ANTITRUST LAW ¶ 229, at 40 (2005 Supp.). And, as a plurality of this Court wrote in *Cantor* v. *Detroit Edison Co.*, 428 U.S. 579, 601-02 (1976), *Noerr* "did not involve any question of either liability or exemption for private action taken in compliance with state law. * * * [N]othing in the *Noerr* opinion implies that the mere fact that a * * * regulatory agency may approve a proposal * * * is a sufficient reason for conferring antitrust immunity on the proposed conduct."

The court of appeals nonetheless agreed with the district court and held that the tobacco company defendants were immune under the *Noerr-Pennington* doctrine not only for their actions in negotiating and seeking court approval of the MSA, but also for their subsequent, non-petitioning conduct under the regime established by the MSA and its related statutes. App. A15. The court acknowledged that the plurality and concurring opinions in *Cantor* suggested that there was no *Noerr-Pennington* immunity for subsequent anticompetitive conduct, even if approved or required by a State, but questioned the precedential value of those opinions. App. A18-A20. Instead, the Ninth Circuit looked to its own and Fifth Circuit precedent to limit *Cantor* and conclude that private parties can indeed be immunized for post-petitioning conduct and not merely for the act of petitioning itself. App. A19-A20.

Erroneously viewing the injuries in this case as stemming exclusively from the state statutes, and ignoring the tobacco companies' coordinated price in-

creases beyond that required to fund the MSA, the court held that the *Noerr-Pennington* doctrine was dispositive of the claims against the private defendants. App. A20-A21. The court recognized that such holding was in tension with the holding of the Second Circuit in *Freedom Holdings I* that the MSA implementing statutes themselves were not protected from preemption by *Noerr-Pennington* immunity, but claimed that defendants were not seeking immunity for the statutes *per se*, merely for their conduct pursuant to or consistent with such statutes. App. A21 n. 9.

c. Regarding the claims against the state Attorney General, the court found that *Parker* state-action immunity applied both to the act of entering into the MSA and to the adoption and enforcement of the related statutes. Entry into the MSA, said the court, qualified as "state action" for *Parker* purposes notwithstanding that the MSA was first devised among the private defendants and only then brought to the state attorneys general for approval of the scheme. App. A21-A23. The court further held that, being "sovereign" state action, neither the MSA nor the related statutes were subject to the *Midcal* requirements of clear articulation and active supervision, but were instead entitled to supposed absolute immunity under *Hoover*. App. A28. Arguing that *Midcal* only applied to claims of immunity by private actors invoking state law as a defense, not to the immunity of state actors themselves, the court concluded that, under *Hoover*, the state "is immune from antitrust liability, regardless of whether the restraint in question would satisfy the *Midcal* test." App. A27-A28.

The court recognized that there was a split on this issue, with the Second and Third Circuits applying the *Midcal* test to reject a claim of *Parker* immunity, and two district courts declining to apply the *Midcal* test and finding immunity under *Hoover*. App. A24 (comparing *Freedom Holdings*, 357 F.3d at 226-32 (applying *Midcal* test) *and Bedell*, 263 F.3d at 259-65 (same) *with PTI, Inc.* v. *Philip Morris, Inc.*, 100 F. Supp.2d 1179, 1195-96 (C.D. Cal. 2000) (rejecting application of *Midcal*) *and S & M Brands, Inc.* v. *Summers*, 393 F. Supp.2d 604, 621-29 (M.D. Tenn. 2005) (same)). The court further expressly rejected the Third Circuit's conclusion in *Bedell* that the MSA was a "hybrid restraint" that failed the *Midcal* test for *Parker* immunity. App. A28-A29 (quoting *Bedell*, 263 F.3d at 258). Relying on its earlier conclusion that the MSA did not delegate any *per se* illegal power "such as the ability to fix prices," the court concluded that "the MSA cannot be classified as a hybrid restraint." App. A30. The court noted its agreement with the Sixth Circuit's similar holding that the MSA scheme was not a hybrid restraint. App. A30 n. 10 (citing *Tritent*, 467 F.3d at 558).

Based on those various holdings, the court thus affirmed the district court's judgment of dismissal.

7. This petition for a writ of certiorari followed.

REASONS FOR GRANTING THE WRIT

This Court should grant the current petition for a writ of certiorari because it presents important issues upon which the circuits are divided. The issues involve a settlement agreement affecting nearly all of the States, millions of consumers, and billions of dol-

lars annually. More generally, the divergent views in the courts of appeals on the scope of *Parker* and *Noerr-Pennington* immunity create considerable uncertainty regarding the antitrust laws in all areas where the States may indirectly facilitate or sanction private anticompetitive schemes, and alters the federalism balance between the federal government and the States acting in concert on matters that affect the entire national economy, not merely the local economy of a particular State.

I. There Is an Extended Split on the Questions Presented.

As the Ninth Circuit repeatedly recognized, the decision below expands a split among the federal courts of appeals on several issues relating to antitrust immunity.

A. The Decision Below Expands the Split on Whether State Statutes Implementing the MSA Are Preempted by Federal Antitrust Law.

The decision below expands an existing split between the Sixth and Second Circuits over whether the MSA and its related statutes are preempted by federal antitrust law. The Ninth Circuit, joining the Sixth, holds that because such statutes do not necessarily mandate or authorize illegal activity "in all cases," they are not preempted. App. A13-A14; *Trident*, 467 F.3d at 557-58.

The Second Circuit, by contrast, has held that because the underlying arrangement among the tobacco companies "would be a *per se* violation because it is a naked restraint on competition," and because the implementing statutes serve to enforce that arrangement and threaten to bolster the scheme into "a per-

manent, nationwide cartel," the statutes are preempted. *Freedom Holdings I*, 357 F.3d at 226.

Both the Sixth and the Ninth Circuits acknowledge the earlier Second Circuit decision and expressly reject its reasoning, App. A14 n. 7; *Tritent*, 467 F.3d at 557-58, making the split both conscious and unlikely to be reconciled without intervention by this Court. The Second Circuit, for its part, denied rehearing and rehearing *en banc* in *Freedom Holdings I*, and issued a further panel opinion in support of the denial of rehearing rejecting a variety of additional arguments by the state defendants. *Freedom Holdings, Inc.* v. *Spitzer*, 363 F.3d 149 (CA2 2004) ("*Freedom Holdings II*"). Since that time the Second Circuit has shown no sign of retreating from its views, and has even allowed a suit challenging the MSA to go forward against 31 state attorneys general, finding personal jurisdiction against them in New York, as the place where they negotiated parts of the MSA and the model Escrow statute. *Grand River Enterprises Six Nations, Ltd.* v. *Pryor*, 425 F.3d 158, 166 (CA2 2005), *cert. denied*, 17 S. Ct. 379 (2006). Rather than reconsidering its position, the Second Circuit is poised to extend it to cover the operation of the MSA in 31 different States.

Accordingly, no benefit would be derived from further delay in resolving the intractable division among the courts of appeals on the validity of the MSA and its implementing legislation. The underlying legal disputes have been well-aired in the conflicting decisions of the Second, Sixth and Ninth Circuits. Future courts will simply pick sides. Moreover, as the decision in *Grand River Enterprises Six Nations* illus-

trates, there exists a real possibility that different circuits will be called upon to pass on the validity of the same state implementing laws, inevitably resulting in conflicting judgments on the validity of the same state laws. Only this Court can resolve the current conflict and avoid that impending chaos.

B. The Decision Below Expands A Split on Whether the Noerr-Pennington *Doctrine, Standing Alone, Immunizes Private Actors for the Anti-Competitive Results of their Petitioning Activity, as Opposed to Merely for the Petitioning Activity Itself.*

The decision below also contributed to growing conflict and confusion over the scope of the *Noerr-Pennington* doctrine.

The *Noerr-Pennington* doctrine generally entitles private parties to seek from the government a law that would restrain trade. On that point there is general agreement. But the question then arises whether, having successfully lobbied for a restraint on trade, a defendant automatically enjoys *Noerr-Pennington* immunity for actions it takes under the authority of that newly enacted state law, or whether the legality of the defendant's conduct is to be judged, instead, under the standards set forth in the *Parker* and its progeny.

In this case, the court of appeals concluded that the question is governed by *Noerr-Pennington* and that a defendant who lobbied for a government restraint on trade is absolutely immune for engaging in anticompetitive conduct authorized by the resulting legislation (and, in this case, settlement agreement). Under that view, it is unnecessary to decide whether

the law is pre-empted under *Midcal* or protected by *Parker*. App. A30 n. 11.

In adopting the same view, the Third Circuit has held that even though the MSA regime does not qualify for *Parker* immunity (because the states do not sufficiently supervise the anticompetitive conduct undertaken pursuant to the settlement), defendants acting under the MSA are nonetheless immune under the *Noerr-Pennington* because the legislation is the result of protected petitioning.[5]

Both this Court and the Second Circuit, however, have properly understood the *Noerr-Pennington* doctrine to extend only to the petitioning activity itself, with the *results* of such petitioning activity evaluated under the *Parker* and *Midcal* tests. The Second Circuit, for example, held in *Freedom Holdings I* that MSA implementing statutes are not entitled to *Noerr-Pennington* protection, notwithstanding that the

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[5] *Bedell*, 263 F.3d at 251-52 ("the petitioner is immune from antitrust liability whether or not the injuries are caused by the act of petitioning or are caused by government action which results from the petitioning"; agreeing with the district court that "defendants engaged in petitioning activity with sovereign states and are immune under the *Noerr-Pennington* doctrine"); *id.* at 258(finding that "just as the injury in *Midcal* was caused by private parties taking advantage of the state imposed market structure, the anticompetitive injury here resulted from the tobacco companies' conduct after implementation of the Multistate Settlement Agreement, and not from any further positive action by the States";); *id.* at 266 (finding that the States "fail the second prong [of the *Midcal* test] requiring them to actively supervise the anticompetitive restraints causing injury. Because private participants in state action enjoy *Parker* immunity only to the extent the States enjoy immunity, the defendants are not shielded by *Parker*.").

MSA may have been the result of protected petitioning, because the resulting legislation failed the *Parker* and *Midcal* tests and, thus, was pre-empted. *See* 357 F.3d at 233 ("[T]he immunity for advocacy cannot sensibly protect the resultant anticompetitive legislation from being held to be preempted as in conflict with the Sherman Act. Otherwise, all such legislation would be immune."); *id.* ("The end product of regulatory legislation can take many forms, some preempted, some not. * * * [Protecting the right to petition] does not, however, protect the ultimate legislative result from Supremacy Clause analysis.").

A plurality of this Court in *Cantor* similarly held that *Noerr*

> did not involve any question of either liability or exemption for private action taken in compliance with state law. * * * [N]othing in the *Noerr* opinion implies that the mere fact that a * * * regulatory agency may approve a proposal * * * is a sufficient reason for conferring antitrust immunity on the proposed conduct.

428 U.S. at 601-02. *See also* 1 Areeda & Hovenkamp, ANTITRUST LAW ¶ 229, at 40 ("*Noerr* protects the petitioning process from antitrust liability, but it does not protect all the results of such petitioning."); *id.* at 40-41 (noting that the wine producers in *Midcal* had petitioned the State for the restrictions in that case, yet the resulting law failed to qualify for state-action immunity and therefore could not immunize the subsequent unsupervised conduct under that law).

By expanding the scope of *Noerr-Pennington* immunity to reach subsequent law and conduct properly analyzed under the *Parker* and *Midcal* state-action

doctrines, the decision below diverges from the holdings of this Court and the Second Circuit in a manner that threatens to undermine the coherent application of both forms of immunity.

C. *The Decision Below Expands the Split on Whether a State Scheme, Enabling Private Antitrust Violations, that Fails the* Midcal *Test Nonetheless Receives* Parker *Immunity.*

In holding that the MSA and its implementing legislation need not be analyzed under the *Midcal* test, the Ninth Circuit acknowledged that it was rejecting the contrary holdings of the Second and Third Circuits, which not only *applied* the *Midcal* test to the MSA and the implementing statutes, but held that the MSA and those statutes *failed* the *Midcal* test and thus were not entitled to *Parker* immunity. App. A28-A29 (rejecting *Midcal* application and analysis in *Freedom Holdings* and *Bedell*). The Ninth Circuit instead joined the holdings of the Sixth Circuit and two district courts in finding that the MSA and its implementing statutes were entitled to immunity without regard to the *Midcal* analysis. App. A24, A30 n. 10 (citing *PTI*, 100 F. Supp.2d at 1195-96; *S&M Brands*, 393 F. Supp.2d at 621-29; and *Tritent*, 467 F.3d at 558).

In *Freedom Holdings I*, however, the Second Circuit correctly recognized that the scheme implemented by the MSA is a "hybrid restraint," not merely a unilateral act by the State. 357 F.3d at 223. The court noted that, unlike laws whereby the State affirmatively and directly regulates or requires private anticompetitive conduct, the "Contraband Statutes allegedly enforce an express market-sharing

agreement among private tobacco manufacturers, the MSA. As alleged in the complaint, the Contraband Statutes are the result of the incentives created by the MSA for the States," and the MSA, in addition to being "an agreement involving the State of New York, * * * also was by any definition a 'contract' that the four major tobacco manufacturers jointly negotiated among themselves." *Id.* at 224. The court thus found that the *Midcal* analysis applied to such a hybrid restraint and that the MSA scheme failed such analysis due to lack of state supervision of the ensuing private anticompetitive behavior. *Id.* at 226, 231-32.

Similarly in *Bedell*, the Third Circuit recognized that "just as the injury in *Midcal* was caused by private parties taking advantage of the state imposed market structure, the anticompetitive injury here resulted from the tobacco companies' conduct after implementation of the [MSA], and not from any further positive action by the States. Even though, as defendants argue, the [MSA] created the cartel, this fact makes the case analogous to *Midcal,* not different." 263 F.3d at 258. The *Bedell* court further concluded that the MSA scheme failed the *Midcal* analysis because the States "lack oversight or authority over the tobacco manufacturers' prices and production levels. These decisions are left entirely to the private actors. Nothing in the [MSA] or its [Escrow] Statutes gives the States authority to object if the tobacco companies raise their prices." *Id.* at 264.

Having expressly considered and rejected the contrary holdings of the Second and Third Circuits, and allied itself with the Sixth Circuit, the court below expanded the existing split on the applicability of the

Midcal analysis to the MSA and its implementing legislation and, more generally, on the applicability of the *Midcal* analysis to any anticompetitive scheme that is implemented, in part or in whole, through state legislation.

II. The Circuit Split Implicates Recurring Questions of National Importance.

This case presents issues of national importance that should be resolved by this Court for a number of reasons.

1. The validity of the MSA, its implementing legislation, and the conduct of the tobacco companies thereunder is a question of great practical importance and recurring litigation.[6] The continuing uncertainty

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[6] *See Tritent Int'l Corp.* v. *Kentucky*, 467 F.3d 547 (CA6 2006); *Xcaliber Int'l Ltd.* v. *Foti*, 442 F.3d 233 (CA5 2006); *Grand River Enterprises Six Nations, Ltd.* v. *Pryor*, 425 F.3d 158, 166 (CA2 2005), *cert. denied*, 17 S. Ct. 379 (2006); *Freedom Holdings, Inc.* v. *Spitzer*, 357 F.3d 205 (CA2), *reh'g denied*, 363 F.3d 149 (2004); *Mariana* v. *Fisher*, 338 F.3d 189 (CA3 2003), *cert. denied*, 540 U.S. 1179 (2004); *A.D. Bedell Wholesale Co.* v. *Philip Morris, Inc.*, 263 F.3d 239 (CA3 2001), *cert. denied*, 534 U.S. 1081 (2002); *Xcaliber Int'l Ltd.* v. *Kline*, No. 05-2261-JWL, 2006 WL 288705 (D. Kan. Feb.7, 2006); *Xcaliber Int'l Ltd.* v. *Edmondson*, No. 04-CV-0922-CVE-PJC, 2005 WL 3766933 (N.D. Okla. Dec.13, 2005); *S & M Brands, Inc.* v. *Summers*, 393 F. Supp.2d 604 (M.D. Tenn. 2005); *PTI, Inc.* v. *Philip Morris, Inc.*, 100 F. Supp.2d 1179 (C.D. Cal. 2000); *Forces Action Project LLC* v. *California*, 2000 WL 20977 (N.D. Cal. 2000) (No. C99-0607 MJJ), *aff'd in part*, 16 Fed. Appx. 774 (CA9 2001) (unpublished); *Premium Tobacco* v. *Fisher*, 51 F. Supp.2d 1099 (D. Colo.1999); *Hise* v. *Philip Morris, Inc.*, 46 F.Supp.2d 1201 (N.D. Okla. 1999), *aff'd mem.*, 208 F.3d 226, 2000 WL 192892 (CA10 2000) (unpublished); *A.B. Coker Co.* v. *Foti*, No. 05-1372 (W.D. La.).

Much of that litigation raises antitrust issues, and even the various constitutional claims being raised, for example under

regarding the legality of the scheme is harmful to all involved. States, in particular, have come to rely on the billions of dollars in funding generated. *See generally* United States General Accounting Office, *Tobacco Settlement: States' Use of Master Settlement Agreement Payments* (June 2001). The continuing unsettled legality of the MSA's funding mechanisms generates harmful uncertainty in state budgeting. At the same time, companies subject to the MSA, or its competitive consequences, face the same uncertainty as they attempt to plan for future operations and investments, a result harmful to both the industry and consumers alike.

Indeed, the States themselves have noted the uncertainty caused by the split over antitrust immunity in a petition to this Court seeking review of the Second Circuit's assertion of jurisdiction over an antitrust claim against 31 state attorney's general. *See* Petition for Writ of Certiorari of State Attorneys General, No. 05-1343, 2006 WL 1049019 (Apr. 18, 2008), seeking review of *Grand River Enterprises Six Nations, Ltd.* v. *Pryor*, 425 F.3d 158 (CA2 2005), *cert. denied*, 17 S. Ct. 379 (2006). In that petition, the Attorney Generals complained that "so long as the Second Circuit's decision stands, petitioners will be denied the certainty and finality that ordinarily results from decisions rendered by federal courts (particularly federal courts of appeals) in their respective States." 2006 WL 1049019, at *14-*15. While this Court, in accordance with its general practice of denying review of interlocutory appeals, denied certiorari

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the Commerce Clause, overlap and interact with the antitrust issues raised.

as to the personal jurisdiction question in *Grand River*, it can resolve much of the States' uncertainty by addressing the substance of the immunity issues in this case (here on final judgment) and providing a uniform national answer.

Moreover, the delay in conclusively resolving the legality of the MSA's anticompetitive effects, and defendants' conduct under it, is prejudicial to consumers who, if petitioner and the Second Circuit are right, are paying billions of dollars in illegally inflated prices every year and foregoing the benefits of the competitive market Congress intended the antitrust laws to encourage. Regardless what this Court might think about the choice to purchase and smoke cigarettes, it remains the case that cigarettes are a legal product whose marketing and sale are subject to the antitrust laws. The strong federal antitrust policy against market division and price-inflating schemes such as this one calls for this Court's intervention to resolve the uncertainty over whether such added costs are being lawfully imposed on consumers. *Cf. Topco*, 405 U.S. at 610 ("Antitrust laws in general, and the Sherman Act in particular, are the Magna Carta of free enterprise. They are as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms.").

2. This case also implicates broader questions of national importance as well. Even setting aside the inherent importance of the legality of the MSA and the anticompetitive conduct that grew out of that agreement, the questions presented here are of general importance to the proper implementation of anti-

trust law generally. As this Court's numerous cases applying *Midcal* demonstrate, industries often successfully petition States to adopt anticompetitive laws that may or may not serve State interests or involve adequate State supervision. *See, e.g., FTC* v. *Ticor Title Ins. Co.*, 504 U.S. 621 (1992); *324 Liquor Corp.* v. *Duffy*, 479 U.S. 335 (1987); *Fisher* v. *City of Berkeley*, 475 U.S. 260 (1986). And circuit and district cases applying *Midcal* to various state laws are too numerous to catalogue.

The court of appeals nonetheless questioned whether *Midcal* remains a "'live' precedent[,]" after *Hoover*, App. A24, and reached a holding that essentially renders that decision a dead letter in most circumstance. Under the Ninth Circuit's approach even if a state law fails scrutiny under *Midcal*, (and therefore, would otherwise be pre-empted), the law and the private conduct thereunder, are nonetheless immune from all challenge – the law is subject to *Parker* protection because it was enacted by the State (whether it meets the *Midcal* criteria or not); and the private conduct is immunized under *Noerr-Pennington* (even if the resulting law is invalid under *Midcal*) because, like all legislation, the otherwise invalid state law was the subject of lobbying by the benefitted group. The range and variety of private schemes that might thus receive the thin cover of State adoption is limited only by the imagination of those who would petition the States for such arrangements.

If *Midcal* is to be overruled, it should be by this Court. As the Ninth Circuit noted, the continued uncertainty as to the validity of *Midcal* and its relationship to *Hoover*, has been a source of confusion in the

lower courts for many years. App. A24. Only this Court can resolve that confusion and restore coherence to the nation's antitrust law.

3. The issues in this case are important for the further reason that the manner in which the States have participated in the MSA – through a multi-state agreement among themselves and the tobacco companies and through coordinated legislation pursuant to that agreement – has serious federalism implications that are themselves of national concern and that are in severe tension with the underpinnings of the *Parker* immunity doctrine. This is not merely a case involving a single State choosing a different economic model for itself, and choosing to forgo competition within its own boundaries. Rather, it involves the combined and coordinated activities of 46 States that impact the nationwide market for cigarettes.

Such coordinated state support for a private anticompetitive scheme seems to fall well outside the federalism values protected by *Parker* immunity doctrine and in fact implicates the precise opposite side of the federalism equation by encroaching upon national authority over a national market. Cf. U.S. Const., art. I, sec. 10 ("No State shall, without the Consent of Congress * * * enter into any Agreement or Compact with another State."); *United States Steel Corp.* v. *Multistate Tax Comm'n*, 434 U.S. 452, 468 (1978) (Compact Clause prohibits States from forming, without congressional consent, "'any combination tending to the increase of political power in the states, which may encroach upon or interfere with the just supremacy of the United States'") (quoting

Virginia v. *Tennessee*, 148 U.S. 503, 519 (1893)). Indeed.

The expansion of antitrust immunity, in the service of a scheme resulting from the a combination among 46 States and the tobacco companies, seems at best an aggressive application of court-made, federalism-based, immunity doctrines and thus warrants closer attention by this Court and its supervision over the application of the doctrines it has created.

III. The Decision Below Improperly Expands Antitrust Immunity Contrary to the Decisions of this Court.

Certiorari is further warranted because the decision below was wrong and in direct conflict with the decisions of this Court.

1. Regarding questions of preemption, the Ninth Circuit erroneously applied the standards for a pre-implementation facial challenge to a statute used by this Court in *Rice* to an as-applied post-implementation challenge to the actual operation of the MSA and its related statutes, a scenario that *Rice* expressly distinguished. *See* 458 U.S. at 658 n. 4 ("[B]ecause respondents brought this suit prior to the effective date of the statute, respondents did not, and could not, challenge any vertical restraints actually employed by a distiller pursuant to the statute. Instead, respondents challenge the statute on its face without consideration of particular circumstances."); *id.* at 661 (applying narrower test for preemption to "a state statute, when considered in the abstract"). Of course, this case does not involve any "abstract" consideration of the MSA and its statutes, but rather

allegations going to the actual operation and effect of that scheme and the private conduct facilitated thereby. Under such circumstances, the approach of the Second Circuit in *Freedom Holdings I* is the appropriate course, and the court should have looked to, and allowed proof of, the "economic realities of the relevant transactions," *United States* v. *Concentrated Phosphate Exp. Ass'n*, 393 U.S. 199, 208 (1968), not merely the hypothetical possibilities that competition might slip through the structure set up by the MSA.

Furthermore, the Ninth Circuit was incorrect in concluding that the MSA and related statutes were mere unilateral state conduct rather than hybrid restraints not entitled to absolute immunity. As described by the Second Circuit, discussed *supra*, at 25-26, the MSA and the related statutes were not simply unilateral state action, they were the result of an *agreement* with and among the major tobacco companies, which agreement effectively coerced state legislatures to adopt the statutes provided for in MSA. That is a classic instance of a hybrid restraint rather than unilateral regulation, and places more in the states in the role of a partner in the agreement, not a sovereign regulator of its subjects. And in that role, the states left the OPMs free to make marketing decisions regarding price increases without supervision, merely enforcing those decisions and insulating the OPMs from the competitive consequences of whatever decisions they collectively made. In order to survive, such a scheme must pass scrutiny under *Midcal*, not merely the blithe assertion that the MSA and its related laws are purely "sovereign" acts.

2. Regarding the *Noerr-Pennington* doctrine, the Ninth Circuit's extension of such First-Amendment-based immunity to ensuing conduct, rather than limiting it to the petitioning activity itself, badly confuses *Noerr-Pennington* immunity with *Parker* state-action immunity, and threatens to render *Midcal* and its progeny meaningless. As described by the Second Circuit, this Court, and the leading treatise on antitrust law, *see supra* at 23-24, merely petitioning for a law does not ensure that such law is entitled to state-action immunity. While anyone may request a potentially invalid law, the mere act of requesting it does not entitle either the State or the requesting party to have that law, and conduct thereunder, immunized from its substantive defects. Indeed, under the Ninth Circuit's approach, *Midcal* itself would have come out differently, and the doctrine therein would be of no continuing use.

A proper understanding of *Noerr-Pennington* immunity extends it only to the petitioning activity itself. Any resulting restraint adopted by the government, and any subsequent private conduct pursuant to that restraint, must be analyzed under the state-action doctrine.

3. Finally, regarding the court's refusal to apply *Midcal* to the state-action immunity question, the court erred for much the same reasons that it erred in its preemption analysis. As already discussed, this case involves, at best, a hybrid restraint subject to *Midcal*. Indeed, the decision by the State Attorney General to enter into the MSA in the first place more closely resembles that officer attempting to make the state "a participant in a private agreement or combi-

nation by others for restraint of trade," *Parker*, 317 U.S. at 351-52, than it does a "sovereign" state act. Indeed, the Attorney General's conduct in agreeing to the MSA would not seem to be a sovereign act at all, but rather the non-sovereign act of a state agent. This Court has only recognized direct sovereign acts of the state in the conduct of the legislature and in the "*legislative*" activities of a state supreme court. *Hoover*, 466 U.S. at 568 (emphasis added). If only the legislative, not the judicial, conduct of a state Supreme Court is considered sovereign state action, than the litigation and contracting activities of a state executive officer would seem to fall far short of the mark.

CONCLUSION

For the reasons above, this Court should grant the petition for a writ of certiorari.

Respectfully submitted,

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Dated: January 25, 2008

APPENDIX A

504 F.3d 903

United States Court of Appeals, Ninth Circuit.

Steve SANDERS, Individually and as Class Representative, Plaintiff-Appellant,

v.

Edmund G. BROWN Jr.,* in his official capacity as Attorney General of the State of California; Philip Morris USA, Inc.; R.J. Reynolds Tobacco Company; Brown & Williamson Tobacco Corp.; Lorillard Tobacco Company, Defendants-Appellees.

No. 05-15676.

Argued and Submitted Feb. 15, 2007.
Filed Sept. 26, 2007.

***906** Appeal from the United States District Court for the Northern District of California; Susan Yvonne Illston, District Judge, Presiding. D.C. No. CV-04-02281-SI.

Before: B. FLETCHER, RICHARD R. CLIFTON, and SANDRA S. IKUTA, Circuit Judges.

CLIFTON, Circuit Judge:

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* Edmund G. Brown Jr. is substituted for his predecessor, Bill Lockyer, as Attorney General of the State of California, pursuant to Fed. R.App. P. 43(c)(2).

This case involves an indirect legal challenge to the massive settlement agreement between the nation's largest tobacco companies and the attorneys general of 46 states and several territories. The 1998 settlement known as the Master Settlement Agreement, or "MSA," resolved all of these states' and territories' claims against those tobacco companies, which the states had sued for billions of dollars in damages related to the harmful effects of smoking.

Plaintiff Steve Sanders, a smoker, alleges that cigarette prices have skyrocketed in the nine years since the MSA, and that the price increases are the result of an illegal price-fixing scheme that the MSA enabled. On behalf of a putative class of cigarette smokers, Sanders sued the Attorney General of the State of California and the four largest tobacco companies: Philip Morris USA Inc., R.J. Reynolds Tobacco Co., Brown & Williamson Tobacco Corp., and Lorillard Tobacco Co.[1] Sanders does not allege that the MSA itself is illegal, but rather alleges that the MSA, the post-MSA price increases, and the state statutes implementing the MSA's terms (the "implementing statutes") are evidence of a cigarette price-fixing cartel that violates the Sherman Act, 15 U.S.C. § 1 *et seq.*; the Cartwright Act, Cal. Bus. & Prof.Code §§ 16720 *et seq.*; other California unfair competition statutes, Cal. Bus. & Prof.Code §§ 17200 *et seq.*; and California's common law of unfair competition. Sand-

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[1] Unless otherwise noted, this opinion will refer to the tobacco companies as "tobacco defendants" and the attorney general as "the State of California." It will use the term "defendants" when referring to both groups collectively.

ers also alleges that the Sherman Act preempts the implementing statutes.

The defendants moved to dismiss under Fed. R.Civ. P. 12(b)(6). The district court granted the motions and dismissed the claims with prejudice. *See Sanders v. Lockyer,* 365 F. Supp.2d 1093 (N.D. Cal. 2005). The district court held that the Sherman Act does not preempt the implementing statutes; that Sanders failed to adequately plead an antitrust violation; and that even if Sanders had done so, the defendants were immune from liability. We affirm.

I. Background

The following facts are undisputed for the purpose of the motion to dismiss, unless otherwise noted. The United States cigarette market is dominated by four companies: Philip Morris USA Inc., R.J. Reynolds Tobacco Co., Brown & Williamson Tobacco Corp., and Lorillard Tobacco Co. Their combined sales have accounted for more than 90 percent of cigarette sales for at least the last decade.

These four companies in the 1990s faced coordinated lawsuits by the attorneys general of most states and U.S. territories, who sought money and other relief to help their governments cope with the harmful effects of smoking and the costs imposed by those effects. In late 1998, the tobacco companies and the attorneys general signed the MSA.[2] State courts, including the California Superior Court, then ap-

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[2] The MSA in its entirety can be found at www.naag.org/backpages/naag/tobacco/msa/msa.pdf (last visited Aug. 23, 2007).

proved *907 the MSA in consent decrees and dismissed the lawsuits against the tobacco companies.

The MSA requires the four major tobacco companies-who, as the initial signatories of the MSA, are known as the "Original Participating Manufacturers"-to pay the states billions of dollars each year. The total annual payments are based on a formula that considers inflation and the total number of individual cigarettes sold in the fifty United States, the District of Columbia and Puerto Rico. Each Original Participating Manufacturer (or "OPM") must annually contribute a portion of the total payment that is equal to the OPM's share of that year's cigarette sales (the OPM's "market share"). For example, if an OPM's market share is 25 percent, that OPM must contribute 25 percent of that year's settlement payment.

The OPMs expected to raise cigarette prices to help pay for the settlement and feared that smaller manufacturers, which were not part of the negotiations, would seize the chance to compete with cheaper cigarettes, possibly cutting into the OPMs' market share. The settling parties addressed this problem in three ways. First, the MSA offered a carrot to non-OPM tobacco companies to join the settlement agreement. These "Subsequent Participating Manufacturers" ("SPMs") could join the settlement within 90 days of the enactment of the MSA. They would not have to make any part of the payments due to the states so long as their market share remained at or below their 1998 market share (or 125 percent of their 1997 market share, whichever was greater). If an SPM's market share increased, however, the SPM

would have to contribute to the settlement payment, with the contribution based on the sales in excess of the SPM's 1998 sales (or 125 percent of 1997 sales, if applicable). For example, if an SPM sold 250,000 cigarettes in 1998, and then one year later sold a larger share of the market-say, 300,000 cigarettes-the SPM would have to contribute to the settlement payment. If the extra 50,000 cigarettes equaled 1 percent of the market share, the SPM would have to pay 1 percent of the settlement payment. As of August 15, 2007, forty-four smaller tobacco companies are participating in the MSA as SPMs.[3]

Second, the OPMs would pay less money under the MSA if their total sales dropped below a certain amount. If the reason for this drop is competition by tobacco companies that did not participate in the MSA, the settlement payment would be reduced even further.

Third, most states have enacted two sets of statutes that allegedly make it harder for non-signatory tobacco companies (and any future market entrants) to undercut the OPMs' and SPMs' market shares. Sanders alleges that the states were motivated to pass these statutes out of fear that the OPMs' higher prices would cause their market share to fall, thereby reducing the amount of the settlement payments to the states. These "implementing statutes" are known in most states as the "Qualifying Act" and the "Contraband Amendment."

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[3] The list can be found on the website of the National Association of Attorneys General, www. naag. org/ backpages/ naag/ tobacco/ msa/ participating_ manu/ (last visited Aug. 22, 2007).

Under the "Qualifying Act," non-signatory tobacco companies (also known as "Non-Participating Manufacturers," or "NPMs") have to pay a portion of their revenues into an escrow account. The money in the escrow account acts as a liability reserve. If the NPMs are successfully sued for cigarette-related harms, *908 the money in the escrow accounts will pay the damage awards. Each NPM's payment is based on market share, and is roughly the same per-cigarette cost as the amount that OPMs must pay to abide by the MSA. The payments can only be used to pay a judgment or settlement on a claim against the NPM, up to the amount that the NPM would otherwise pay under the MSA. Any remaining funds in the escrow account revert back to the NPM after twenty-five years.

This law allegedly prevents the NPMs from undercutting the prices of OPMs' cigarettes by taking away the extra profitability that an NPM would enjoy. For example, say that OPMs' sales are such that for a given year, they must pay 25 cents per cigarette to the states under the MSA. This would seem to give NPMs a cost advantage of 25 cents per cigarette. But under the Qualifying Act, if an NPM also sold cigarettes that year, the NPM would have to pay roughly 25 cents per cigarette into an escrow account, which the NPM could not touch for 25 years. In other words, the NPM's cost advantage over the OPMs is erased.

The "Contraband Amendment," for its part, penalizes NPMs who refuse to make escrow payments under the Qualifying Act. The Contraband Amendment allows a state to "de-list" NPMs from a list of approved tobacco manufacturers. De-listing effectively

prevents the offending NPM from selling cigarettes in that state.

The California legislature has enacted a Qualifying Act and a Contraband Amendment. Cal. Health & Safety Code §§ 104556, 104557 (Qualifying Act); Cal. Bus. & Prof.Code § 22979(a), (b), and Cal. Rev. & Tax Code § 30165.1(d), (e) (Contraband Amendment).

As expected, the OPMs' cigarette prices rose when the MSA took effect. Sanders alleges, however, that the price increases have far exceeded the tobacco companies' costs of complying with the MSA. The OPMs allegedly raised their prices by $12.20 per carton between late 1998 and early 2002-more than twice the amount necessary to meet the OPMs' obligations under the MSA. Also, the price increases have been "parallel." Whenever one OPM has raised its cigarette prices, the others have generally matched the increase. Despite these increases, the OPMs' cigarette sales still account for more than 90 percent of the market.

The price increases and other factors have prompted several legal challenges against the MSA, most alleging antitrust and constitutional violations. The challenges have been largely unsuccessful. *See, e.g., Tritent Int'l Corp. v. Kentucky,* 467 F.3d 547 (6th Cir. 2006); *Mariana v. Fisher,* 338 F.3d 189 (3d Cir. 2003); *A.D. Bedell Wholesale Co. v. Philip Morris Inc.,* 263 F.3d 239 (3d Cir. 2001); *Xcaliber Int'l Ltd. v. Kline,* No. 05-2261-JWL, 2006 WL 288705 (D. Kan. Feb.7, 2006); *Xcaliber Int'l Ltd. v. Edmondson,* No. 04-CV-0922-CVE-PJC, 2005 WL 3766933 (N.D. Okla. Dec.13, 2005); *S & M Brands, Inc. v. Summers,* 393 F. Supp.2d 604 (M.D. Tenn. 2005); *PTI, Inc. v. Philip*

Morris Inc., 100 F. Supp.2d 1179 (C.D. Cal. 2000); *Forces Action Project LLC v. California*, No. C99-0607 MJJ, 2000 WL 20977 (N.D. Cal. Jan.5, 2000), *aff'd in relevant part*, 16 Fed. Appx. 774 (9th Cir.2001) (unpublished disposition); *Hise v. Philip Morris Inc.*, 46 F.Supp.2d 1201 (N.D. Okla.1999), *aff'd*, 208 F.3d 226 (10th Cir. 2000) (unpublished disposition). *But see Freedom Holdings Inc. v. Spitzer*, 357 F.3d 205 (2d Cir. 2004).

II. The Present Case

Sanders alleges that the MSA has spawned a "cartel" because it lets the participating tobacco companies "raise prices without fear of losing sales or market ***909** share." Sanders does not allege that the tobacco companies have agreed amongst themselves to fix prices. Instead, he alleges that the MSA penalizes tobacco companies for competing on price, because they have to pay more money under the MSA as their market shares increase. As a result, tobacco companies allegedly will be reluctant to increase market share. Thus, when one tobacco company raises its prices, all other tobacco companies allegedly can raise prices in lockstep without fearing that their rivals will try to undercut them. "[I]n effect," the complaint alleges, "the OPMs have agreed to compensate each other [f]or any market share increase ... by imposing a proportionate increase in the settlement payment for such market share gain."[4]

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[4] It is not clear that a proportionate price increase, which would not affect the per-cigarette cost of doing business, would dissuade a tobacco company from attempting to increase its market share. We need not, however, address the merits of this claim, as the following discussion will show.

Sanders also alleges that the MSA encouraged other tobacco companies to join the cartel. Any company that has joined the MSA as an SPM will be reluctant to increase its market share beyond 1998 levels, because by doing so it would be forced to pay some money to the states.[5] As a result, the SPMs followed the OPMs when they increase their prices.

Sanders further alleges that the MSA encouraged the states to pass anti-competitive laws protecting the alleged cartel from price competition. This is because the OPMs' payments to the states drop if their total sales drop below a threshold level, or if non-signatory NPMs take away OPMs' market share. The states, Sanders alleges, therefore passed the Qualifying Acts and Contraband Amendments to keep NPMs from entering the market.

The sum of these parts, Sanders alleges, is an illegal "horizontal output-restriction cartel" in which the OPMs, backed by state authority (or, at least, state acquiescence), have raised cigarette prices to artificially high (or "supracompetitive") levels without fear of price competition. This scheme is preempted by the Sherman Act, Sanders argues, because it so obviously conflicts with federal antitrust law. Furthermore, Sanders argues that even if the scheme consisting of the MSA and its implementing statutes is not facially preempted, the tobacco defendants have still commit-

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[5] It is not clear whether this extra payment would really dissuade the SPM from seeking extra market share. If an SPM would pay to the states less money than it would make by selling extra cigarettes, an SPM still might turn a higher profit by increasing its market share. Again, we need not address the merits of this claim.

ted illegal price-fixing, as evidenced by the parallel price increases. Finally, Sanders argues that the State of California failed to adequately supervise the tobacco companies' pricing actions.[6]

***910** The defendants filed motions to dismiss, arguing, among other things, that they are immune to antitrust liability under either (1) the *Noerr-Pennington* immunity doctrine, described in *E. R.R. Presidents Conf. v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 135-145, 81 S.Ct. 523, 5 L.Ed.2d 464 (1961), and *United Mine Workers of America v. Pennington*, 381 U.S. 657, 669-70, 85 S.Ct. 1585, 14 L.Ed.2d 626 (1965); or (2) the "state action" immunity doctrine that originated in *Parker v. Brown*, 317 U.S. 341, 350-52, 63 S.Ct. 307, 87 L.Ed. 315 (1943).

The district court granted the motions to dismiss. *See Sanders*, 365 F.Supp.2d at 1105. The district court held that the Sherman Act did not preempt the

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[6] The relief Sanders seeks includes:

(1) A declaratory judgment that California's Qualifying Act and Contraband Amendment are both "facially void as a *per se* restraint of trade," and therefore preempted by the Sherman Act.

(2) An injunction against the state to keep it from enforcing the MSA and the implementing statutes, and against the tobacco defendants to make them "cease their anticompetitive activity taken in furtherance of the MSA."

(3) Money damages against the tobacco defendants for operating an illegal price-fixing cartel.

Sanders's complaint also seeks to enjoin implementation of the "anticompetitive provisions" of the MSA. His appeal, however, does not address whether the MSA itself is illegal. Sanders instead argues that the MSA is one part of a larger illegal scheme. We therefore need not address whether the MSA itself would be legal in the absence of the alleged larger scheme.

MSA implementing statutes because those statutes do not authorize any *per se* illegal activity. *See id.* at 1101. The district court also held that the state action immunity doctrine protected the defendants from suit because the MSA and its implementing statutes were formed by sovereign state acts that cannot be challenged under federal antitrust law. *See id.* at 1098-1101, 1103-05. The district court further held that the defendants were entitled to *Noerr-Pennington* immunity because their acts of negotiating and entering into the MSA constituted protected speech. *See id.* at 1101-03. Finally, the district court held that Sanders's state law claims failed because the defendants were immune to those claims as well. *See id.* at 1104-05.

III. Analysis

A dismissal under Rule 12(b)(6) is reviewed *de novo. See Knievel v. ESPN,* 393 F.3d 1068, 1072 (9th Cir. 2005). All allegations of fact are taken as true. *See id.* Conclusory allegations and unreasonable inferences, however, are insufficient to defeat a motion to dismiss. *See Cholla Ready Mix, Inc. v. Civish,* 382 F.3d 969, 973 (9th Cir.2004); *Warren v. Fox Family Worldwide, Inc.,* 328 F.3d 1136, 1139 (9th Cir. 2003).

Review is generally limited to the contents of the complaint, but a court can consider a document on which the complaint relies if the document is central to the plaintiff's claim, and no party questions the authenticity of the document. *See Warren,* 328 F.3d at 1141 n. 5. We therefore can analyze the MSA, which is obviously central to the claim, in evaluating the strength of Sanders's allegations.

A. Preemption

Sanders argues that California's Qualifying Act and Contraband Amendment are preempted by Section 1 of the Sherman Act, which states that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce ... is declared to be illegal." 15 U.S.C. § 1. To be preempted by this Act, a state statute must be in "irreconcilable" conflict with the federal antitrust regulatory scheme. *Rice v. Norman Williams Co.*, 458 U.S. 654, 659, 102 S.Ct. 3294, 73 L.Ed.2d 1042 (1982). The only way such a conflict can exist, according to the Supreme Court, is if the state statute "mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party" to violate those laws. *Fisher v. City of Berkeley*, 475 U.S. 260, 265, 106 S.Ct. 1045, 89 L.Ed.2d 206 (1986) (quoting *Rice*, 458 U.S. at 661, 102 S.Ct. 3294) (internal quotation marks omitted). A conflict that is "hypothetical or potential" is "insufficient" to warrant preemption. *Rice*, 458 U.S. at 659, 102 S.Ct. 3294. Thus, a state statute is only preempted by the Sherman Act "when the conduct contemplated by the statute is in all cases a ***911** *per se* violation. If the activity addressed by the statute does not fall into that category ... the statute cannot be condemned in the abstract." *Id.* at 661, 102 S.Ct. 3294.

Neither the Qualifying Act nor the Contraband Amendment explicitly allow price fixing, market division, or other *per se* illegal monopolistic behavior. Sanders argues, however, that these statutes create such high barriers to NPMs' market entry and ability

to price-compete that they have "virtually guaranteed collusion and monopoly prices in the cigarette market." (Quoting 1 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law,* ¶ 226(a), at 35 (2006 Supp.)). The statutes therefore place irresistible pressure on all cigarette companies to fix prices, Sanders argues.

The statutes do place some pressure on some new entrant tobacco companies to charge higher prices if they decide to enter the market. The Qualifying Act forces NPMs to place into escrow a per-cigarette payment roughly equal to the per-cigarette payment that participating manufacturers pay under the MSA. The Contraband Amendment prevents NPMs who fail to make the escrow payments from distributing their cigarettes. If NPMs wish to remain profitable, they must factor the escrow payments into the prices they charge per cigarette. The statutes thus may cause higher prices and dissuade some potential market entrants. Nothing, however, forces the NPMs to either peg their prices to those of participating manufacturers, or to refrain altogether from entering the market. If the OPMs really are charging artificially high prices, and thus making artificially high profits, an NPM conceivably could compete on price by charging a "normal" price and still make a "normal" profit, even taking the escrow payment into account.

Sanders therefore has failed to adequately allege that the implementing statutes mandate or authorize conduct that "in all cases" violates federal antitrust law. *See Fisher,* 475 U.S. at 265, 106 S.Ct. 1045 (quoting *Rice,* 458 U.S. at 661, 102 S.Ct. 3294) (inter-

nal quotation marks omitted). The implementing statutes are thus not preempted by the Sherman Act. *See, e.g., Tritent,* 467 F.3d at 557-58 (holding that Kentucky statutes implementing the MSA in that state were not preempted because they did not mandate or authorize illegal activity "in all cases").[7]

B. Immunity

Sanders next argues that even if the Sherman Act does not preempt the implementing statutes, the tobacco companies have nonetheless violated the Act by using the MSA and implementing statutes to create a price-fixing cartel. The state of California, for its part, has allegedly fostered this cartel either by passing the implementing ***912** statutes and thus encouraging price-fixing, or at least by failing to prevent it from happening.

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[7] The Second Circuit has held that the MSA and its companion statutes are preempted by federal law. *See Freedom Holdings,* 357 F.3d at 222-32. The *Freedom Holdings* opinions (both the original and the denial of the petition for rehearing) feature forceful economic arguments on how tobacco companies could potentially use the MSA and its companion statutes to minimize price competition and keep new entrants out. The court concludes that the "alleged arrangement, even without the protection of the Contraband Statutes ... would be a *per se* violation because it is a naked restraint on competition.... With the Contraband Statutes in force, the scheme as alleged threatens to become a permanent, nationwide cartel." 357 F.3d at 226.*Freedom Holdings,* however, ignores the *Rice* requirement that the statute "in all cases" mandate *per se* illegal conduct. The Sixth Circuit in *Tritent* disagreed with *Freedom Holdings* for that very reason. *Tritent,* 467 F.3d at 557-58. We agree with the Sixth Circuit and, likewise, decline to follow the Second Circuit's approach.

The defendants argue that Sanders has failed to allege any conduct that would violate the Sherman Act. The defendants also argue that even if Sanders has adequately pleaded Sherman Act violations, they are nonetheless immune from prosecution under the *Noerr-Pennington* immunity doctrine, the state action doctrine, or both.

1. ***Noerr-Pennington* immunity**

The tobacco defendants argue that their acts of (1) negotiating the MSA, (2) petitioning the California courts for approval of the MSA, and finally (3) acting according to the MSA's terms, are constitutionally protected from antitrust liability under the *Noerr-Pennington* immunity doctrine.

The *Noerr-Pennington* doctrine arises from two Supreme Court cases, *E. R.R. Presidents Conf. v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 135-145, 81 S.Ct. 523, 5 L.Ed.2d 464 (1961), and *United Mine Workers of America v. Pennington*, 381 U.S. 657, 669-70, 85 S.Ct. 1585, 14 L.Ed.2d 626 (1965). The Court, citing First Amendment and federalism concerns, held that private actors are immune from antitrust liability for petitioning the government, even when the private actors' motives are anticompetitive. *Noerr-Pennington* immunity protects petitions to all departments of the government. *See Cal. Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508, 510, 92 S.Ct. 609, 30 L.Ed.2d 642 (1972); *Kottle v. Northwest Kidney Ctrs.*, 146 F.3d 1056, 1059 (9th Cir. 1998).

The Supreme Court has interpreted "petitioning" to encompass activities other than legislative lobbying. For example, *Noerr-Pennington* immunity protects private actors when they file court documents

and enter contracts with the government. *See Trucking Unlimited,* 404 U.S. at 510, 92 S.Ct. 609;*see also Greenwood Utilities Comm'n. v. Mississippi Power Co.*(*Greenwood Utilities*), 751 F.2d 1484, 1505 (5th Cir.1985).

Neither the Supreme Court nor the Ninth Circuit have specifically held that a settlement agreement like the MSA qualifies as "petitioning" that may be protected by *Noerr-Pennington* immunity. The Seventh Circuit, however, has explicitly held that *Noerr-Pennington* immunity protects private parties from liability for negotiating and entering into settlements or other agreements with the government. *See Campbell v. City of Chicago,* 823 F.2d 1182, 1186-87 (7th Cir.1987). We now join that circuit in so holding.

In *Noerr,* the Supreme Court reasoned that petitioning of government officials deserved immunity from antitrust liability for two reasons. 365 U.S. at 137-38, 81 S.Ct. 523. First, allowing liability for such petitions would "substantially impair the power of [state] government to take actions through its legislature and executive that operate to restrain trade." *Id.* at 137, 81 S.Ct. 523. Second, "[t]he right of petition is one of the freedoms protected by the Bill of Rights," and nothing in the Sherman Act indicated an intent to "invade" that freedom. *Id.* at 138, 81 S.Ct. 523. Furthermore, the Court concluded that it is inappropriate to base liability on whether a petitioner has an anticompetitive motive, because that would unduly chill speech:

> It is inevitable, whenever an attempt is made to influence legislation by a campaign of publicity, that an incidental effect of that

> campaign may be the infliction of some direct injury upon the interests of the party against whom the campaign is directed. And it *913 seems equally inevitable that those conducting the campaign would be aware of, and possibly even pleased by, the prospect of such injury. To hold that the knowing infliction of such injury renders the campaign itself illegal would thus be tantamount to outlawing all such campaigns.

Id. at 143-44, 81 S.Ct. 523.

The act of negotiating a settlement with a state undoubtedly is a form of speech directed at a government entity. Given the Court's desire to protect free speech from Sherman Act attack, it is clear why *Noerr-Pennington* immunity should protect a private party from liability for such an act. If a person undertaking to negotiate a way out of his legal troubles were to fear that the very act of negotiating would expose him to further liability, he might be afraid to attempt a settlement in the first place. The result would be fewer settlements, even when the parties would otherwise be willing to reach a principled compromise, and more cases dragging on for years to the detriment of all parties, not to mention the court system.

Furthermore, holding that a private party's settlements with the government are exposed to antitrust liability would surely, as the Supreme Court in *Noerr* warned, "substantially impair the power of [state] government to take actions through its legislature and executive that operate to restrain trade." *Id.* at 137, 81 S.Ct. 523. If a state can restrain trade

through its "legislature and executive," that means the attorney general, an executive officer, can negotiate trade restraints in the context of litigation, so long as those restraints are not preempted by the Sherman Act.

We therefore hold that *Noerr-Pennington* immunity protects a private party from liability for the act of negotiating a settlement with a state entity.[8] Immunity thus protects the tobacco defendants from liability for the act of negotiating the MSA with the State of California.

Sanders argues that even if *Noerr-Pennington* immunity protects the defendants from liability for the MSA itself, it does not protect the tobacco defendants from liability for increasing prices after the MSA. Sanders bases his argument on the plurality opinion in *Cantor v. Detroit Edison Co.*, 428 U.S. 579, 96 S.Ct. 3110, 49 L.Ed.2d 1141 (1976). In *Cantor,* a private utility gave free light bulbs to customers, an act that allegedly harmed light bulb retailers. *See id.* at 581-82, 96 S.Ct. 3110. Even though the free-bulb program had technically been "approved" by state regulators-it was included in the utility's proposed rate plan-the plurality declined to extend *Noerr-Pennington* immunity to the program. The plurality said that "nothing in the *Noerr* opinion implies that the mere fact that a state regulatory agency may approve a proposal ... and thereby require that the pro-

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[8] We do not address whether *Noerr-Pennington* immunity may protect an anticompetitive settlement agreement between two *private* entities, who conceivably could claim that the act of petitioning the court to accept their agreement immunizes the agreement itself.

posal be implemented ... is a sufficient reason for conferring antitrust immunity on the proposed conduct." *Id.* at 601-02, 96 S.Ct. 3110. Justice Blackmun, concurring separately, said he agreed with the plurality "insofar as it holds that the fact that anticompetitive conduct is sanctioned, or even required, by state law does not of itself put that conduct beyond the reach of the Sherman Act."*Id.* at 605, 96 S.Ct. 3110 (Blackmun, J., concurring in the judgment).

Subsequent cases cast doubt on the precedential value of this fragmented opinion. The Court itself undercut the *Cantor* ***914** plurality in *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 108 S.Ct. 1931, 100 L.Ed.2d 497 (1988), in which the Court stated that "'where a restraint upon trade or monopolization is the result of valid governmental action, as opposed to private action,' those urging the governmental action enjoy absolute immunity from antitrust liability for the anticompetitive restraint." *Id.* at 499, 108 S.Ct. 1931 (quoting *Noerr*, 365 U.S. at 136, 81 S.Ct. 523) (internal alteration omitted).

The lower courts have also interpreted *Cantor* narrowly. In *Greenwood Utilities*, the Fifth Circuit held that *Cantor* "cannot support" a broad rule that *Noerr-Pennington* immunity never extends to the consequences of government acts that result from immunized petitioning. *See* 751 F.2d at 1504. Such a rule would weaken *Noerr-Pennington*, the Fifth Circuit held: "First Amendment petitioning privileges would indeed be hollow if upon achieving a petitioned-for end the petitioner were then subjected to antitrust liability for his success." *Id.* at 1505. The Fifth Circuit distinguished *Cantor* because, in that case, the pri-

vate actor (not the government) had independently created the restraint. *See id.* at 1504. The Fifth Circuit therefore held that *Noerr-Pennington* immunity extends to restraints that are created by the government in response to private-party petitions, as long as those restraints are "not simply government approval of private conduct." *Id.*; *see also Bonollo Rubbish Removal, Inc. v. Town of Franklin*, 886 F. Supp. 955, 965 (D.Mass.1995) ("A *Noerr-Pennington* doctrine which shielded a private party in its attempt to secure a benefit from the government but left the party open to suit if the benefit was actually received would not serve the interests of free speech and open access to government that the *Noerr* and *Pennington* Courts intended to protect.").

For our part, we have followed *Allied Tube* and explicitly held that *Noerr-Pennington* immunity protects a private party from liability not only for the petition, but also for any injuries that result "directly" from valid government action taken on the petitioner's behalf. *Sessions Tank Liners, Inc. v. Joor Mfg., Inc.*, 17 F.3d 295, 299 (9th Cir.1994). This rule is dispositive of Sanders's case, to the extent the injury he alleges-supracompetitive cigarette prices-resulted directly from the action of the State of California, that is, from "the MSA and the Attorney General's enforcement of the escrow statute and contraband statute." Although subsequent agreements by the defendants to engage in the "operation of an output cartel" might not be immune from liability under this rule, Sanders's complaint does not allege any such subsequent agreement in restraint of trade. Therefore, because Sanders's complaint is based on

injuries caused directly by government action, *Noerr-Pennington* immunity shields the tobacco defendants from liability for the alleged supracompetitive price increases.[9] Since Sanders's claim against the tobacco defendants is predicated on these price increases, his claim against the tobacco defendants must fail.

2. State action immunity

The State of California, for its part, argues that state action immunity, or ***915** "*Parker* immunity," protects it from liability both for entering into the MSA and for enacting the implementing statutes. We agree.

The *Parker* immunity doctrine protects most state laws and actions from antitrust liability. The doctrine originated in *Parker v. Brown,* 317 U.S. 341, 350-52, 63 S.Ct. 307, 87 L.Ed. 315 (1943). In *Parker,* the Court dismissed a Sherman Act challenge to a California law that restricted competition among raisin manufacturers. The Court held that nothing in the Sherman Act suggests its purpose is "to restrain a state or its officers or agents from activities directed by its legislature." *Id.* at 350-51, 63 S.Ct. 307. Thus, even a state law that would violate the Sherman Act is immune from attack on antitrust grounds. *See id.* The only exception to this rule is a state law that at-

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[9] The Second Circuit in *Freedom Holdings* found that the MSA implementing statutes were not themselves protected by *Noerr-Pennington* immunity because "the immunity for advocacy cannot sensibly protect the resultant anticompetitive legislation from being held to be preempted as in conflict with the Sherman Act. Otherwise, all such legislation would be immune." 357 F.3d at 233. This holding may be correct, but the defendants here do not claim that *Noerr-Pennington* immunity protects the implementing statutes from preemption.

tempts to "give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Id.* at 351, 63 S.Ct. 307.

The Supreme Court has never specified what conduct comprises a state action that is "directed" by the state legislature and is therefore immune. In post-*Parker* cases, however, the Supreme Court has articulated some general tests to help decide whether a particular action qualifies for *Parker* immunity. A threshold question, therefore, is whether a court approved settlement like the MSA may be protected by *Parker* immunity. The next question is whether the MSA scheme in particular meets the Supreme Court criteria for *Parker* immunity.

The answer to the first question is clear under our court's precedents. If a government entity enters into a settlement like the MSA, the settlement is a "state action" that may be protected by *Parker* immunity. We have held that *Parker* covers not only state legislation, but also the acts of courts and executive-branch officials. *See Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, Inc.*, 810 F.2d 869, 876 (9th Cir.1987); *Deak-Perera Hawaii, Inc. v. Dept. of Transportation*, 745 F.2d 1281, 1283 (9th Cir.1984). The MSA in particular seems to involve several state actions. To begin with, the lawsuits against the tobacco defendants were initially filed by the states. Even though private tobacco companies initiated the settlement negotiations, the California attorney general ultimately approved the MSA, and the state court approved the settlement in a consent decree

and final judgment. The MSA thus fits the basic definition of "state action" for *Parker* purposes.

The second question-whether the MSA scheme meets all the criteria for *Parker* immunity-is considerably more complex. Even though the MSA is probably a state act, it does not necessarily qualify for *Parker* immunity from antitrust liability. A series of Supreme Court cases holds that any action in restraint of trade is only immune if it satisfies a two-part test: The anticompetitive policy not only must be (1) "clearly articulated and affirmatively expressed as state policy," but also must be (2) "actively supervised by the state itself." *Cal. Retail Liquor Dealers Ass'n. v. Midcal Aluminum, Inc.* (*Midcal*), 445 U.S. 97, 105, 100 S.Ct. 937, 63 L.Ed.2d 233 (1980) (quoting *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389, 410, 98 S.Ct. 1123, 55 L.Ed.2d 364 (1978) (plurality opinion)) (internal quotation marks omitted); *see also 324 Liquor Corp. v. Duffy*, 479 U.S. 335, 343-44, 107 S.Ct. 720, 93 L.Ed.2d 667 (1987); *Patrick v. Burget*, 486 U.S. 94, 100, 108 S.Ct. 1658, 100 L.Ed.2d 83 (1988); *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 631, 112 S.Ct. 2169, 119 L.Ed.2d 410 (1992). Other Supreme Court cases, however, explicitly hold that a state's own ***916** acts in the antitrust area are always immune; these cases suggest that the two-part "*Midcal* test" is only needed to decide whether private conduct pursuant to a state statute gets *Parker* immunity. In other words, a state need not show it "actively supervises" private parties, as long as the state itself, acting as sovereign, created the restraint of trade. *See Hoover v. Ronwin*, 466 U.S. 558, 568-69, 104 S.Ct. 1989, 80 L.Ed.2d 590 (1984); *City of Co-*

lumbia v. Omni Outdoor Advertising, Inc., 499 U.S. 365, 377-79, 111 S.Ct. 1344, 113 L.Ed.2d 382 (1991).

It is unclear whether *Hoover* and *Midcal* are coexisting "live" precedents, or whether one overrules the other. It is possible that the *Midcal* test is limited, as *Hoover* suggests, to cases in which the courts must decide whether private conduct is actually protected "state action." The *Midcal* line of cases, however, never mentions the *Hoover* line of cases, even though they chronologically overlap. Indeed, *324 Liquor*, which was decided after *Hoover*, explicitly states that the way a state statute gets *Parker* immunity is by satisfying the two-part *Midcal* test. *See* 479 U.S. at 343-44, 107 S.Ct. 720. Since *324 Liquor* never mentions *Hoover*, it is unclear whether the Supreme Court was saying that even sovereign state acts must meet the *Midcal* test (therefore overruling *Hoover* without saying so) or merely applying the *Midcal* test in an appropriate circumstance (by analyzing whether private conduct gets *Parker* immunity).

Whether the *Midcal* test applies to the MSA is a critical question for the present case. The lower courts have split on whether the MSA should get *Parker* immunity, chiefly because some apply *Midcal*, and some-following the *Hoover* precedent-do not. *Compare Bedell*, 263 F.3d at 259-65 (applying the *Midcal* test and finding no *Parker* immunity); *Freedom Holdings*, 357 F.3d at 226-32 (same), *with PTI*, 100 F.Supp.2d at 1195-96 (citing *Hoover*, declining to apply *Midcal*, and holding that *Parker* immunity protects defendants from liability); *S & M Brands*, 393 F.Supp.2d at 621-29 (same).

Sanders argues that the *Midcal* test is appropriate here and reasons that since California has never "actively supervised" the tobacco defendants' price increases, state action immunity protects none of the defendants from antitrust liability. The defendants, however, argue that the *Midcal* test is inappropriate because the MSA and the implementing statutes were "sovereign acts," and that under *Hoover,* the MSA, the Qualifying Act and the Contraband Amendment are automatically immune from suit.

Our circuit precedent indicates that the defendants are correct. In *Deak-Perera Hawaii,* we held that a state "acting as sovereign" is "immune from the federal antitrust laws." 745 F.2d at 1282 (internal citations and quotation marks omitted). We distinguished *Midcal* by noting that "this is not a case of private parties imposing competitive restraints in conjunction with state authorities. In such a case the inquiry would be different." *Id.* at 1283; *see also Charley's Taxi,* 810 F.2d at 875-76 (following *Deak-Perera*).

Nonetheless, Sanders argues that the *Midcal* line of cases have overruled *Hoover,* and that *Deak-Perera* and *Charley's Taxi* therefore are dead precedents. Sanders points to Ninth Circuit cases that, like the *Midcal* line of cases, apply the *Midcal* test without considering the *Hoover* rule that sovereign state acts are *per se* immune. *See, e.g., Snake River Valley Elec. Ass'n. v. Pacificorp,* 238 F.3d 1189, 1192-95 (9th Cir.2001). Even though these cases might be read to shed some doubt on *Hoover*'s viability, we conclude that the *Hoover* rule survives both logical ***917** scrutiny and a semantic parsing of the *Midcal* cases.

First, it makes no sense to apply the *Midcal* test to a sovereign state act. *Midcal* holds that an anticompetitive restraint is protected under *Parker* only if the state "actively supervise[s]" the anticompetitive conduct. 445 U.S. at 105, 100 S.Ct. 937. *Parker,* however, appears to extend immunity from antitrust liability to all government officers' acts if those acts are "directed by [a state's] legislature." 317 U.S. at 350-51, 63 S.Ct. 307. If the *Midcal* test applied to those government officers' acts, it would dramatically narrow the scope of immunized acts to those in which the government took an active role in supervising the marketplace. Rigid pricing schemes in which the state government itself sets prices for products, and enforces penalties on those who violated the controls, might be immune from antitrust liability, but gentler schemes that restrained competition without engaging in onerous "active supervision" might be illegal. Such a rule appears to conflict with a key holding of *Parker*: that the Sherman Act is not intended to interfere with state attempts to impose market restraints. *See Parker,* 317 U.S. at 350-51, 63 S.Ct. 307.

Second, the holding in *Hoover* is broader than the holdings in the *Midcal* line of cases. The Court in *Hoover* said that "[t]he starting point in *any* analysis involving the state-action doctrine is the reasoning of *Parker v. Brown.*" 466 U.S. at 567, 104 S.Ct. 1989 (emphasis added). Since *Parker* held that state acts are immune from antitrust liability, the *Hoover* Court reasoned, "[w]here the conduct at issue is in fact that of the state legislature or supreme court, we need not address the issues of 'clear articulation' and 'active supervision.' "*Id.* at 569, 104 S.Ct. 1989. "Closer

analysis" is only required "when the activity at issue is not directly that of the legislature or supreme court, but is carried out by others pursuant to state authorization." *Id.* at 568, 104 S.Ct. 1989. In short, *Hoover* clearly states that the *Midcal* test does not apply to sovereign state acts, which are immune from antitrust liability so long as they avoid preemption by authorizing *per se* illegal activities.

Midcal, however, makes no such blanket statements. In that opinion, the Court was chiefly concerned with how to distinguish between a private price-fixing scheme and an immunized state act. Indeed, each of the *Midcal* line of cases involved a private body-not a state-making anticompetitive decisions under the aegis of a state regulatory scheme. In *Midcal* and *324 Liquor,* the Court considered whether state-authorized pricing schemes for wholesale alcohol, which gave price-fixing control to private parties, had enough active state supervision to qualify for *Parker* immunity. *Midcal,* 445 U.S. at 103-06, 100 S.Ct. 937; *324 Liquor,* 479 U.S. at 342-45, 107 S.Ct. 720. In *Ticor,* the Court examined whether states had given too much leeway to title search companies to set their own rates. 504 U.S. at 632-40, 112 S.Ct. 2169. And in *Patrick v. Burget,* the Court analyzed a state-authorized, but privately-run, medical review board that allegedly restricted competition among doctors. 486 U.S. at 99-106, 108 S.Ct. 1658.

Furthermore, the Supreme Court has repeatedly hinted that the *Midcal* test is limited only to situations in which private bodies operate under state regulatory authority. In *Southern Motor Carriers Rate Conf., Inc v. United States,* 471 U.S. 48, 105

S.Ct. 1721, 85 L.Ed.2d 36 (1985), the Court stated that *Midcal*'s two-pronged test is "applicable to private parties' claims of state action immunity," but said nothing about whether the test applied to sovereign ***918** state acts. 471 U.S. at 61, 105 S.Ct. 1721. In *Ticor,* the Court clarified that in *Midcal,*"we announced the two-part test *applicable to instances where private parties participate in a price-fixing regime.*"504 U.S. at 633, 112 S.Ct. 2169 (emphasis added).

Hoover therefore controls in cases where the state, acting as a sovereign, imposes restraints on competition. The state in such situations is immune from antitrust liability, regardless of whether the restraint in question would satisfy the *Midcal* test.

Since the California attorney general's act of entering into the MSA is a sovereign act, as are the legislature's actions in enacting the Qualifying Act and Contraband Amendment, the state is immune from antitrust liability for these actions, unless the MSA scheme is an attempt to "give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Parker;* 317 U.S. at 351, 63 S.Ct. 307. The MSA and the implementing statutes authorize no illegal activity, as we discussed above in analyzing whether the implementing statutes are preempted. *See* Part III.A *supra.* We therefore hold that *Parker* immunity protects the state from antitrust liability for entering into the MSA and for passing the implementing statutes.

In so holding, we recognize that we disagree with two other circuits. The Second Circuit in *Freedom*

Holdings and the Third Circuit in *Bedell* applied the *Midcal* analysis and held that *Parker* immunity does not protect the state from liability for entering into the MSA. *Freedom Holdings,* 357 F.3d at 226-32; *Bedell,* 263 F.3d at 259-66. As discussed above, however, we believe the *Midcal* analysis would only be appropriate if the MSA is not a sovereign act, which we conclude it is.

We also reject the *Bedell* Court's conclusion that the MSA is not a sovereign state act, but rather resembles a "hybrid restraint" existing somewhere outside the realm of *Parker* immunity. *Bedell,* 263 F.3d at 258. To explain why we disagree, it is necessary to briefly touch on the concept of a "hybrid restraint."

A hybrid restraint is one form of state law that is illegal *per se* under the Sherman Act. *See Fisher,* 475 U.S. at 267-270, 106 S.Ct. 1045. A hybrid restraint exists when the state creates "nonmarket mechanisms [that] merely enforce private marketing decisions." *Id.* at 267-68, 106 S.Ct. 1045. In other words, it exists when the state passes laws that enforce companies' decisions to collude on prices, to dictate prices by which other companies must abide, or to otherwise violate the Sherman Act.

Ninth Circuit and Supreme Court cases provide a few examples of hybrid restraints. Each of these cases hinged on a state's decision to let producers dictate market conditions to others-for example, by "posting" prices that then became legally binding on buyers and other producers. *See id.* at 268-69, 106 S.Ct. 1045 (characterizing as hybrid restraints the price-posting schemes that had been the subjects of *Midcal* and of *Schwegmann Bros. v. Calvert Distillers*

Corp., 341 U.S. 384, 71 S.Ct. 745, 95 L.Ed. 1035 (1951)); *see also 324 Liquor*, 479 U.S. at 345 n. 8, 107 S.Ct. 720 (noting that a New York law allowing liquor wholesalers to fix their own prices could be called a hybrid restraint); *Miller*, 813 F.2d at 1349-51 (finding a hybrid restraint where a statutory scheme let wholesalers set prices that retailers were legally bound to honor).

Such a scheme necessarily involves a delegation of market power to private parties that is *per se* illegal under the Sherman ***919** Act. *See Miller*, 813 F.2d at 1349-51 (*citing Fisher*, 475 U.S. at 267-68, 106 S.Ct. 1045). Otherwise, the hybrid restraint could not be attacked as facially invalid. As we have already discussed, the MSA involves no such delegation of *per se* illegal power such as the ability to fix prices. *See* Part III.A *supra*. We must therefore conclude that the MSA cannot be classified as a hybrid restraint.[10] Accordingly, we decline to follow the Third Circuit and instead hold that the state is entitled to *Parker* immunity in this case.[11]

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[10] The Sixth Circuit, in *Tritent*, reached a similar conclusion about the Kentucky version of the MSA scheme. The Sixth Circuit held that the *Rice v. Norman Williams Co.*, 458 U.S. 654, 102 S.Ct. 3294, 73 L.Ed.2d 1042 (1982), preemption analysis "must precede the analysis under the hybrid-restraint theory." *Tritent*, 467 F.3d at 558. Since the plaintiffs in *Tritent* had failed to demonstrate preemption, the Sixth Circuit declined to hold that the Kentucky version of the MSA scheme was a hybrid restraint. *Id.*

[11] The tobacco defendants argue that they, too, are entitled to *Parker* immunity. We need not reach this issue, since we have already held that they are entitled to immunity under the *Noerr-Pennington* doctrine.

C. State law claims

Sanders also brought claims under California antitrust law. California courts have held that the *Noerr-Pennington* immunity doctrine applies to protect private petitioners of the government from state-law antitrust liability in exactly the same way as it protects them from federal antitrust liability. *See Blank v. Kirwan,* 39 Cal.3d 311, 216 Cal.Rptr. 718, 703 P.2d 58, 63-65 (1985). Since *Noerr-Pennington* immunity shields the tobacco defendants from Sherman Act liability, it also shields them from state antitrust liability. *See PTI,* 100 F. Supp.2d at 1196.

As for the State of California's liability under its own laws, the district court correctly noted that the California legislature could hardly have violated its own statutes by passing another statute. *See Sanders,* 365 F. Supp.2d at 1104-05. Furthermore, the California courts have held that political divisions of the State of California are not subject to the Cartwright Act, which means that the state cannot be held liable for entering into the MSA. *See Blank,* 216 Cal. Rptr. 718, 703 P.2d at 65.

D. Conclusion

Sanders has failed to show that the MSA implementing statutes are *per se* illegal under the Sherman Act. Sanders also has failed to show that any of the defendants are liable under either the Sherman Act or under California antitrust law. Sanders therefore has failed to state a claim entitling him to relief, and the district court properly dismissed his lawsuit.

AFFIRMED.

APPENDIX B

365 F. Supp.2d 1093

United States District Court, N.D. California.

Steve SANDERS, individually and as class representative, Plaintiff,

v.

Bill LOCKYER, in his official capacity as Attorney General of the State of California; Philip Morris USA, Inc.; R.J. Reynolds Tobacco Company; Brown & Williamson Tobacco Corporation; and Lorillard Tobacco Company, Defendants.

No. C 04-02281 SI.

March 28, 2005.

ORDER GRANTING DEFENDANTS' MOTIONS TO DISMISS

ILLSTON, District Judge.

On January 12, 2005, this Court heard oral argument on motions to dismiss brought by defendant Bill Lockyer ("Lockyer") and defendants Philip Morris USA, Inc., R.J. Reynolds Tobacco Company, Brown & Williamson Tobacco Corporation, and Lorillard Tobacco Company (collectively "manufacturer defendants"). Having carefully considered the arguments of counsel and the papers submitted, the Court hereby GRANTS defendants' motions for the reasons set forth below.

BACKGROUND

This case arises out of the Master Settlement Agreement ("MSA") entered into on November 23, 1998, between the four leading domestic cigarette manufacturers and the attorneys general of forty-six states, including California.[1] The MSA and related legislation have been subject to multiple legal challenges, and two different district courts in this circuit have rejected such challenges. *See PTI, Inc. v. Philip Morris, Inc.*, 100 F. Supp.2d 1179 (C.D. Cal. 2000); *Forces Action Project LLC v. California*, 2000 WL 20977 (N.D. Cal. 2000).[2]

Under the MSA, the states agreed to dismiss pending suits and to refrain from filing suit against the four cigarette manufacturers, and the manufacturers

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[1] The District of Columbia and five U.S. territories are also parties to the MSA. *See* Compl. Ex. A, Master Settlement Agreement § II(rr).

[2] Other unsuccessful legal challenges to the MSA include *Premium Tobacco v. Fisher*, 51 F. Supp.2d 1099 (D. Colo.1999); *Hise v. Philip Morris, Inc.*, 46 F.Supp.2d 1201 (N.D. Okla. 1999), *aff'd mem.*, 208 F.3d 226, 2000 WL 192892 (10th Cir. 2000); *A.D. Bedell Wholesale Co. v. Philip Morris, Inc.*, 104 F.Supp.2d 501 (W.D. Pa. 2000), *aff'd*, 263 F.3d 239 (3d Cir. 2001), *cert. denied*, 534 U.S. 1081, 122 S.Ct. 813, 151 L.Ed.2d 697 (2002). In *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205 (2d Cir. 2004), *reh'g denied*, 363 F.3d 149 (2d Cir. 2004), the Second Circuit reversed the district court's dismissal of an action brought against New York state officials challenging MSA-related legislation, finding that state action immunity doctrine did not immunize the legislation from preemption by the Sherman Act. On remand, the district court denied plaintiffs' motion for a preliminary injunction with regard to the MSA, New York's "escrow statute," and the Contraband statute. *See Freedom Holdings, Inc. v. Spitzer*, 2004 WL 2035334 at *31, 2004 U.S. Dist. LEXIS 18296 at *101 (2004).

agreed to pay billions of dollars to the states over a number of years, to be used to pay health costs from smoking-related illnesses and to fund smoking prevention programs. *1096 These four manufacturers also agreed to numerous restrictions regarding sales, marketing, advertising, lobbying, research, education, and disclosure practices. MSA § III. Courts in the settling states issued consent decrees and final judgments approving the MSA.

The four manufacturer defendants in this case, Philip Morris USA Inc., R.J. Reynolds Tobacco Company, Brown & Williamson Tobacco Corporation, and Lorillard Tobacco Company, are referred to in the MSA as the "Original Participating Manufacturers," or OPMs. Under the MSA, the OPMs are required to make annual payments to the settling states based on their relative market shares. Other cigarette manufacturers existing at the time of the MSA were given ninety days to elect to participate in the MSA. Those who did are called "Subsequent Participating Manufacturers," or SPMs. An SPM is subject to the same marketing restrictions as the OPMs but guaranteed a permanent exemption from the annual payment requirement as long as its market share remains below 1998 levels or 125% of 1997 levels, whichever is greater. MSA § IX(i). Plaintiff alleges that the OPMs and SPMs account for at least 96% of all U.S. cigarette sales. Compl. ¶ 18. Manufacturers electing not to participate in the MSA are called "Non-Participating Manufacturers," or NPMs. NPMs are not subject to any marketing restrictions.

Plaintiff Steve Sanders represents a class of California consumers who purchased cigarettes manufac-

tured by one or more of the manufacturer defendants from June 9, 2000, to the present. Compl. ¶ 6. Plaintiff challenges the MSA as an "anticompetitive hybrid agreement" that permits the OPMs and SPMs to prevent price competition and raise cigarette prices. Compl. ¶ 3, 20. Plaintiff also alleges that the manufacturer defendants have "further protect[ed] their market dominance" by "obtain[ing] the passage of two California statutes" and have dramatically increased the price of cigarettes since the enactment of the MSA. *Id.* According to plaintiff, the MSA creates a cartel accomplished through several of its provisions: (1) the Relative Market Share Adjustment; (2) the Renegade Clause; (3) the NPM Downward Adjustment; (4) the Qualifying Acts; (5) the Contraband Amendments; and (6) the Severability Clause.

The Relative Market Share Adjustment provides that each individual manufacturer defendant's share of the annual payment obligation is based on its relative market share.[3] Plaintiff alleges that the Relative Market Share Adjustment restricts output and eliminates price competition because if one OPM raises prices, the others will be "induced and/or coerced" into following the price increase, since any increase in market share will be offset, exceeded, or substantially reduced by increased payment obligations. Compl. ¶ 21.

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[3] The MSA defines "market share" as a manufacturer's "respective share (expressed as a percentage) of the total number of individual Cigarettes sold in the fifty United States, the District of Columbia and Puerto Rico during the applicable calendar year." MSA § II(z).

The Renegade Clause permanently exempts an SPM from making annual payments as long as its market share remains below 1998 or 125% of 1997 levels. For each increase in market share, an SPM is penalized by having to pay a pro rata share of the annual payment. Thus, plaintiff alleges that the Renegade Clause effectively prevents SPMs from price competing with the manufacturer defendants by penalizing SPMs that increase their market share and offsetting the profits an SPM can get from additional sales. Compl. ¶ 22.

The NPM Downward Adjustment compensates manufacturer defendants for any *1097 loss in market share due to "disadvantages" associated with participating in the MSA, including price competition with a NPM. In some circumstances, the manufacturer defendants' payment obligation may be decreased up to three times the amount of revenue lost, which coerces states to protect the manufacturer defendants' market share so as not to suffer this reduction in revenue. Compl. ¶ 23. According to plaintiff, the states have enacted laws that protect the MSA's anti-competitive provisions, specifically the Qualifying Acts and Contraband Amendments, and these statutes are preempted by federal antitrust laws.[4]

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[4] Defendant Lockyer refers to the "Qualifying Act" as the "reserve fund statute." Under the MSA, a Qualifying Act is one that is substantively identical to the Model Statute set forth in the agreement. MSA Ex. T. He refers to the "Contraband Amendment" as "California's 'complementary legislation.' " Def. Lockyer's Mot. at 8:18-19. The Court uses the language of the complaint and thus refers to these statutes as the Qualifying Act and Contraband Amendment.

The Qualifying Act aims to "effectively and fully neutralize[ ] the cost disadvantages that the Participating Manufacturers experience vis-a-vis Non-Participating Manufacturers." MSA §IX(d)(2)(E).[5] The Qualifying Act creates a barrier to entry for cigarette manufacturers who did not begin selling cigarettes until after 1998. These manufacturers "have no practical choice" but to become NPMs, since without 1997 or 1998 market share they cannot benefit from the permanent payment exception of SPMs. Compl. ¶ 27(a)(1). As NPMs, these manufacturers pay a percentage of each unit sale into escrow, forcing them to set prices higher than SPMs. The escrow payments discourage price competition with the OPMs and SPMs. The Contraband Amendment, a subsequent amendment to the Qualifying Act, permits the Attorney General to prevent a tobacco manufacturer from selling cigarettes in California if the manufacturer is not complying with the Qualifying Act.

Plaintiff alleges that the manufacturer defendants have used the MSA, the Qualifying Act, and the Contraband Amendment to protect their market shares while they price gouge California consumers. Specifically, plaintiff contends that the OPMs raised the price of a carton of cigarettes by $4.50 on the day the MSA was enacted, and by $7.70 per carton in the three and a half years since then, earning an additional $20 billion per year in revenue. Compl. ¶ 29. Plaintiff alleges that the OPMs' market shares "have not appreciably changed" despite these price in-

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[5] California's Qualifying Act is Cal. Health & Safety Code § 104557. The Contraband Amendment is Cal. Bus. & Prof.Code § 22979.

creases. *Id.* at ¶ 30. In addition, the State of California does not supervise the OPMs' pricing decisions. *Id.* at ¶ 29.

Plaintiff seeks declaratory relief under 28 U.S.C. § 2201 against defendant Lockyer; injunctive relief under 42 U.S.C. § 1983 against defendant Lockyer; and injunctive relief under the Sherman Antitrust Act, 15U.S.C. § 1, against all defendants, on grounds that the statutes implementing the MSA are preempted by federal antitrust laws. Plaintiff also seeks damages from the manufacturer defendants for violations of Cal. Bus. & Prof.Code §§ 16720, Cal. Bus. & Prof.Code §§ 17200, common law unfair competition, and restitution.

Now before the Court are motions to dismiss the complaint by defendant Lockyer and the manufacturer defendants.[6]

***1098 LEGAL STANDARD**

Under Federal Rule of Civil Procedure 12(b)(6), a district court must dismiss a complaint if it fails to state a claim upon which relief can be granted. The question presented by a motion to dismiss is not whether the plaintiff will prevail in the action, but whether the plaintiff is entitled to offer evidence in support of the claim. *See Scheuer v. Rhodes,* 416 U.S. 232, 236, 94 S.Ct. 1683, 40 L.Ed.2d 90 (1974) (overruled on other grounds by *Davis v. Scherer,* 468 U.S. 183, 104 S.Ct. 3012, 82 L.Ed.2d 139 (1984)).

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[6] Plaintiff and defendant Lockyer have filed Requests for Judicial Notice ("RJN"). Defendants object to plaintiff's RJN on grounds of relevance. The Court finds that the materials submitted by plaintiff are relevant, and hereby GRANTS both parties' requests.

In answering this question, the court must assume that the plaintiff's allegations are true and must draw all reasonable inferences in the plaintiff's favor. *See Usher v. City of Los Angeles,* 828 F.2d 556, 561 (9th Cir. 1987). Even if the face of the pleadings suggests that the chance of recovery is remote, the Court must allow the plaintiff to develop the case at this stage of the proceedings. *See United States v. City of Redwood City,* 640 F.2d 963, 966 (9th Cir. 1981).

If the court dismisses the complaint, it must then decide whether to grant leave to amend. The Ninth Circuit has "repeatedly held that a district court should grant leave to amend even if no request to amend the pleading was made, unless it determines that the pleading could not possibly be cured by the allegation of other facts." *Lopez v. Smith,* 203 F.3d 1122, 1130 (9th Cir. 2000) (citations and internal quotation marks omitted).

DISCUSSION

I. Lockyer's Motion to Dismiss

The first three claims against defendant Lockyer challenge the validity and enforceability of California's Qualifying Act and Contraband Amendment, as *per se* violations of federal antitrust law subject to preemption by the Sherman Antitrust Act, 15U.S.C. § 1 et seq. Lockyer moves to dismiss plaintiff's first, second, and third causes of action against him on grounds that (1) the state-action immunity doctrine protects California's legislation implementing the MSA; and (2) even if this immunity does not apply, California's Qualifying Act and Contraband Amendment are not preempted by federal antitrust law. In addition, Lockyer contends that, to the extent that

plaintiff is challenging the MSA itself, the *Noerr-Pennington* doctrine bars plaintiff's claims.

A. State action immunity

The state action doctrine, first enunciated by the Supreme Court in *Parker v. Brown,* 317 U.S. 341, 350-52, 63 S.Ct. 307, 87 L.Ed. 315 (1943), provides that when a state exercises its authority and enacts a regulation with anti-competitive effects, the state and private parties acting at its direction are not liable for antitrust violations. *See PTI v. Philip Morris, Inc.,* 100 F. Supp.2d at 1196. The doctrine is based on principles of federalism and state sovereignty, and the *Parker* court reasoned that Congress did not intend the Sherman Act to restrain the conduct of state officials acting at the direction of the legislature. *Parker,* 317 U.S. at 350-51, 63 S.Ct. 307. The doctrine does not apply when the state acts as a "participant in a private agreement or combination by others for restraint of trade." *Id.* at 351-52, 63 S.Ct. 307. In addition, "a state does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Id.* at 351, 63 S.Ct. 307. The *Parker* doctrine has been extended from pure legislative activity to action by the judicial and executive branches, as well as to the regulatory acts of municipalities that are authorized by state law. *See Hoover v. Ronwin,* 466 U.S. 558, 573, 104 S.Ct. 1989, 80 L.Ed.2d 590 (1984) (state supreme court was immune ***1099** from antitrust liability for regulating state bar admissions); *Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, Inc.,* 810 F.2d 869, 876 (9th Cir.1987) (state executives and agencies may be entitled to immunity for

actions pursuant to their constitutional or statutory authority); *City of Columbia v. Omni Outdoor Adver.*, 499 U.S. 365, 370-74, 111 S.Ct. 1344, 113 L.Ed.2d 382 (1991) (municipality immune under *Parker* when authorized by state law to set billboard restrictions).

Since *Parker*, the Supreme Court has clarified the state action doctrine. In *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 100 S.Ct. 937, 63 L.Ed.2d 233 (1980), it articulated "two standards for antitrust immunity": (1) the challenged restraint must be "clearly articulated and affirmative expressed as state policy"; and (2) the state must "actively supervise" the policy. *Midcal*, 445 U.S. at 105, 100 S.Ct. 937 (citations omitted). Then, in *Hoover v. Ronwin, supra*, the Supreme Court further held that "when a state legislature adopts legislation, its actions constitute those of the State, and *ipso facto* are exempt from the operation of the antitrust laws." *Hoover*, 466 U.S. at 567-68, 104 S.Ct. 1989. Reviewing its state action jurisprudence, the court observed:

> In cases involving the anticompetitive conduct of a nonsovereign state representative the Court has required a showing that the conduct is pursuant to a "clearly articulated and affirmatively expressed state policy" to replace competition with regulation. The Court has also found the degree to which the state legislature or supreme court supervises its representative to be relevant to the inquiry. When the conduct is that of the sovereign itself, on the other hand, the danger of unauthorized restraint of trade does not arise. Where the con-

> duct at issue is in fact that of the state legislature or supreme court, we need not address the issues of "clear articulation" and "active supervision."

Hoover, 466 U.S. at 569, 104 S.Ct. 1989 (citations omitted).

Thus, after *Midcal* and *Hoover,* the threshold inquiry is whether the challenged action is a sovereign act by the state or the conduct of private persons.

Here, Lockyer contends that California's Qualifying Act and Contraband Amendment are sovereign acts by the state of California, enacted by the legislature and enforced by politically accountable state officials. Plaintiff argues that the MSA and these legislative enactments together require *Midcal* analysis because the statutes are not exempt from antitrust scrutiny simply because they are sovereign acts of the state.[7] Applying *Midcal,* plaintiff contends that the MSA fails to meet the requirement that the state "actively supervise" the anticompetitive activity.

The Court finds that the settlement itself is a sovereign act of the state of California, and the Qualifying Act and the Contraband Amendment are direct legislative activity. As the *PTI* court recognized, the MSA is the product of litigation by the states' attorneys general and then negotiation with the major tobacco companies. It was approved in California by a judgment and consent decree in the California Superior Court. *See* Def. Lockyer's Mot. Ex. B. The Cali-

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[7] Plaintiff also argues that *Midcal* analysis is appropriate because the MSA is a "hybrid restraint." The Court considers this argument in Part II, below.

fornia legislature enacted the Qualifying Act in 1999 and the Contraband Amendment in 2003. *Parker* makes clear that legislative enactments are direct state action, and under *Hoover,* the *Midcal* analysis is neither appropriate nor required for direct acts of the sovereign. In addition, ***1100** the Ninth Circuit has expressly held that executive branch officials are entitled to *Parker* immunity "for actions taken pursuant to their constitutional or statutory authority, regardless of whether these particular actions or their anticompetitive effects were contemplated by the legislature." *Charley's Taxi,* 810 F.2d at 876; *see also Deak-Perera Hawaii, Inc. v. Dep't of Transp.,* 745 F.2d 1281, 1282-83 (9th Cir. 1984).

In *Charley's Taxi,* the challenged action was an exclusive contract to provide airport taxi services, with a maximum rate set by city ordinance. The Ninth Circuit found that "[w]hen the state executive or executive agencies act within their lawful authority, their acts are those of the sovereign," and did not address the active supervision requirement of *Midcal.* Plaintiff argues that *Charley's Taxi* is distinguishable because the government set the rates and prices, and that it no longer remains good law.

The Court is persuaded that *Charley's Taxi* remains good law and that the application of its rule by the district courts in this circuit was correct. *See PTI v. Philip Morris, Inc.,* 100 F.Supp.2d 1179; *Forces Action Project LLC v. State of California,* No. 99-0607 MJJ, Order Denying Leave to Amend at 8-9 & n. 12 (Manufacturer Defs.' Mot. Ex. A). The *Forces Action* court concluded that the Supreme Court's decision in *F.T.C. v. Ticor Title Ins. Co.,* 504 U.S. 621, 112 S.Ct.

2169, 119 L.Ed.2d 410 (1992) did not overrule *Charley's Taxi*, and that therefore even if the immunity recognized by the Ninth Circuit was broader than in other circuits, it was bound by the Ninth Circuit's decision. *See Forces Action Project*, Order Denying Leave to Amend at n. 12. This Court concurs in that assessment. Accordingly, defendant Lockyer is immunized under the state action doctrine from antitrust liability for the MSA itself and for enforcement of the Qualifying Act and Contraband Amendments.

The Second Circuit's contrary holding does not persuade the Court otherwise.[8] In *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, 233, *reh'g denied*,

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[8] In addition, the Court declines to follow the Third Circuit's pronouncements on this issue, which are equivocal at best. In *A.D. Bedell Wholesale Co. v. Philip Morris*, 263 F.3d 239 (3d Cir. 2001), *cert. denied*, 534 U.S. 1081, 122 S.Ct. 813, 151 L.Ed.2d 697 (2002), the Third Circuit affirmed the dismissal of claims brought against cigarette manufacturers on the basis of the *Noerr-Pennington* doctrine. The *Bedell* court also applied *Midcal* analysis and concluded that the manufacturers were not entitled to *Parker* immunity. 263 F.3d at 254. Although the *Bedell* court did not reach the question of "whether the acts of executive officials constitute state action that avoids *Midcal* analysis," 263 F.3d at 256, the Third Circuit later addressed this issue in *Mariana v. Fisher*, 338 F.3d 189 (3d Cir. 2003), *cert. denied*, 540 U.S. 1179, 124 S.Ct. 1413, 158 L.Ed.2d 80 (2004). It considered itself "bound by *Bedell* to abstain from reaching a different conclusion on *Parker* immunity," and by *Bedell's* statement that "because private participants in state action enjoy *Parker* immunity only to the extent the States enjoy immunity, the defendants are not shielded by *Parker*." It observed: "[p]erhaps unintentionally, because the issue was not before it, by this sentence *Bedell* seems to have assumed, if not decided, that the States have no *Parker* immunity," and noted that "[c]ritics may with some justification regard our discussion of *Parker* immunity as dictum, and well it may be." 338 F.3d at 203-04.

363 F.3d 149 (2d Cir. 2004), that Court of Appeals applied *Midcal* analysis and held that the alleged anti-competitive scheme was not actively supervised by the state of New York. The *Freedom Holdings* court considered *Hoover* inapplicable because the anticompetitive conduct in *Hoover* was performed entirely by state actors, but this Court finds that the principle enunciated in *Hoover* and *Parker* reaches beyond *Hoover's* facts. In light of this Supreme ***1101** Court authority and the apparent scope of state action immunity in the Ninth Circuit, the Court finds that defendant Lockyer is immune from antitrust liability under *Parker*.

Accordingly, the Court hereby GRANTS Lockyer's motion to dismiss on this ground.

B. Preemption analysis

Lockyer also argues that *Midcal* analysis is inappropriate because California's legislation is not, as plaintiff alleges in his first three causes of action, preempted by the Sherman Act. Preemption may exist if the challenged scheme constitutes a *per se* violation of the Sherman Act. A challenged state statute is a *per se* violation if, on its face, it "mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute." *Rice v. Norman Williams Co.*, 458 U.S. 654, 661, 102 S.Ct. 3294, 73 L.Ed.2d 1042 (1982). As with any inquiry regarding whether a state law is preempted by a federal statute under the Supremacy Clause, the fundamental question is "whether there exists an irreconcilable conflict between the federal and state

regulatory schemes." *Id.* at 659, 102 S.Ct. 3294. The existence of a "hypothetical or potential conflict is insufficient to warrant the preemption of the state statute." *Id.*

Lockyer contends that there is no conflict here because the challenged statutes do not permit tobacco manufacturers to fix prices, limit output, divide markets, or engage in violations of the antitrust laws. The Court agrees. The key allegation of plaintiff's Sherman Act claim is that the MSA creates an incentive for the manufacturer defendants to raise prices in parallel fashion, since a price increase by one OPM alone would increase market share for the others as well as for the SPMs, resulting in their having to make higher payments under the settlement. This scenario presents a "hypothetical" or "potential" conflict with the Sherman Act, but not the "irreconcilable" conflict required for preemption. The California statutes do not mandate, permit, or place irresistible pressure on manufacturers to take concerted action; rather they require unilateral action by each to make settlement or escrow payments. The statutes themselves also constitute action on the part of the California legislature, not concerted action by private parties in restraint of trade, as the Sherman Act requires. *See* 15 U.S.C. § 1. In addition, as Lockyer contends, the alleged barrier to entry for NPMs created by the Qualifying Act is not apparent from the face of the statute. Taking all of plaintiff's allegations as true, the Court cannot conclude that the MSA authorizes collusive or concerted action on the part of the manufacturers to raise prices to monopolistic levels.

Consequently, the Court finds that the MSA does not constitute a *per se* violation of the Sherman Act.

C. *Noerr-Pennington* immunity

According to Lockyer, Sanders' complaint appears only to challenge California's legislation implementing the MSA, not the MSA itself. But in the event that plaintiff seeks relief from Lockyer based on the MSA, defendant argues that this claim is barred by *Noerr-Pennington* immunity.

The *Noerr-Pennington* doctrine protects from antitrust liability those who petition the government in order to secure or amend their rights. *See E. R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 81 S.Ct. 523, 5 L.Ed.2d 464 (1961); *1102 *United Mine Workers of America v. Pennington*, 381 U.S. 657, 85 S.Ct. 1585, 14 L.Ed.2d 626 (1965). The doctrine encompasses the right to petition all branches of government, including the judiciary, *see Cal. Motor Transp. Co. v. Trucking Unlimited*, 404 U.S. 508, 92 S.Ct. 609, 30 L.Ed.2d 642 (1972), but does not include sham or baseless petitioning. *Omni*, 499 U.S. at 379-80, 111 S.Ct. 1344; *Prof. Real Estate Investors, Inc. v. Columbia Pictures Indus.*, 508 U.S. 49, 60-61, 113 S.Ct. 1920, 123 L.Ed.2d 611 (1993). Under *Noerr-Pennington*, private entities are immune from liability for "mere attempts to influence the passage or enforcement of laws." *Noerr*, 365 U.S. at 135, 81 S.Ct. 523. The immunity exists regardless of the potentially anti-competitive motivations of the private actors. *Pennington*, 381 U.S. at 670, 85 S.Ct. 1585. The doctrine applies to government officials' petitioning activity in addition to

that of private parties. *Manistee Town Center v. City of Glendale,* 227 F.3d 1090, 1093 (9th Cir. 2000).

The issue for Lockyer is whether *Noerr-Pennington* applies only to the acts of petitioning themselves or whether it extends to the resulting government action, including a litigation settlement like the MSA. *Noerr-Pennington* immunizes certain conduct "incidental to the prosecution of the suit," which includes the decision to settle a claim. *See Theofel v. Farey-Jones,* 359 F.3d 1066, 1078 (9th Cir. 2004); *Columbia Pictures Indus., Inc. v. Prof'l Real Estate Investors, Inc.,* 944 F.2d 1525, 1528 (9th Cir. 1991), *aff'd,*508 U.S. 49, 113 S.Ct. 1920, 123 L.Ed.2d 611 (1993). Moreover, other courts have found that "incidental" conduct includes litigation settlements and the MSA in particular. *See Bedell,* 263 F.3d at 252 (reasoning that *Noerr-Pennington* immunity applies to settlement agreements between private parties and sovereign states "as it does to other more traditional petitioning activities"); *PTI,* 100 F. Supp.2d at 1193 (finding immunity for the MSA itself and for "the various Qualifying States, versions of the Model Act, trademark litigation, and anticompetitive conduct of the private defendants"); *Hise,* 46 F. Supp.2d at 1206 (finding that private defendants' conduct in negotiating and entering into the MSA was incidental to litigation), *aff'd mem.,*208 F.3d 226, 2000 WL 192892 (10th Cir. 2000); *Forces Action Project LLC v. California,* 2000 WL 20977, at *8 (N.D. Cal. Jan. 5, 2000) (finding *Noerr-Pennington* immunity for the actions of government and tobacco company defendants in entering into the MSA). This Court agrees that *No-*

err-Pennington immunity applies to the MSA as the direct result of protected petitioning activity.

Accordingly, the Court hereby GRANTS defendant Lockyer's motion to dismiss.

II. Manufacturer Defendants' Motion to Dismiss

The manufacturer defendants move to dismiss plaintiff's third, fourth, fifth, sixth, and seventh causes of action against them, arguing that all claims are barred by both the *Noerr-Pennington* and *Parker* immunity doctrines.

A. *Noerr-Pennington* immunity

The manufacturers argue that all of the conduct alleged in Sanders' complaint is immunized under the *Noerr-Pennington* doctrine. As discussed above, *Noerr* immunity protects efforts by private actors to influence public officials, regardless of their anticompetitive motivations. *Omni,* 499 U.S. at 380, 111 S.Ct. 1344; *Pennington,* 381 U.S. at 670, 85 S.Ct. 1585. Plaintiff contends that while *Noerr-Pennington* applies to the manufacturers' activities in negotiating and achieving the MSA, there is no immunity for "the subsequent operation of an anticompetitive restraint." Pl.'s Opp'n at 10:26-27. He argues that *Noerr-Pennington* protects only petitioning conduct ***1103** of the manufacturer defendants, and that the MSA and related legislation are merely "fruits" of the petitioning activity not covered by the doctrine.

Every district court to consider the application of *Noerr-Pennington* to the MSA and related statutes has concluded that the conduct of the tobacco manufacturers in negotiating and entering into the settlement is immunized under the doctrine. *See PTI,* 100

F.Supp.2d at 1193 ("the private defendants are clearly immune for their activities involved with the negotiation, execution, and attempts to implement the MSA, the Qualifying Statute, and the Model Act"); *Forces Action Project,* 2000 WL 20977 at *8 ("defendants action in negotiating and entering into the MSA are immunized from suit"); *Hise,* 46 F.Supp.2d at 1206 ("defendants' activities, in negotiating the MSA with the several settling states and achieving a settlement agreement with those states, are protected under the *Noerr-Pennington* doctrine"); *Bedell,* 263 F.3d at 250-54 (affirming district court on this ground).[9] In addition, Ninth Circuit law has not changed since *PTI* and *Forces Action* were decided.

The Court cannot conclude that *Noerr-Pennington* immunity is limited in the manner plaintiff suggests. While the Ninth Circuit has not yet ruled on whether the doctrine can immunize anticompetitive restraints resulting from petitioning activity, several courts have expressly held that parties are immune from liability for antitrust injuries caused by the petitioned-for government action. *See, e.g., Bedell,* 263 F.3d at 252; *PTI,* 100 F.Supp.2d at 1193 (finding immunity for "[a]ll claims premised on the illegality of the MSA § under the antitrust laws"); *Forces Action Project,* Order Denying Leave to Amend at 9 ("[i]t is well-settled that the *Noerr-Pennington* doctrine applies to immunize entities where, as here, no First Amend-

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[9] While *Freedom Holdings* holds that *Noerr-Pennington* does not apply, it involved only a suit against New York state officials, not tobacco manufacturers, and a challenge to the MSA enabling statutes, not the MSA itself. Thus, it is not relevant to the manufacturers' motion.

ment rights are implicated and the alleged conduct would be deemed illegal *per se* under the antitrust laws"). This principle was also recognized by the Supreme Court in *Pennington. See* 381 U.S. at 669, 85 S.Ct. 1585. Moreover, plaintiff's argument that immunizing the fruits of petitioning activity would make all legislation immune is unavailing. To the contrary, the immunity would mean nothing if a petitioner "were then subjected to antitrust liability for his success." *Greenwood Utilities Comm'n v. Mississippi Power Co.,* 751 F.2d 1484, 1505 (5th Cir.1985); *see also Campbell v. City of Chicago,* 823 F.2d 1182 (7th Cir.1987). Plaintiff does not allege, and the Court does not find, that the settlement itself is a "sham," and thus the MSA is covered by *Noerr-Pennington.* The distinction plaintiff seeks to draw-between defendants' conduct in negotiating and achieving the settlement and their subsequent compliance with its regime-is one without a difference in this case.

The Court finds that *Noerr-Pennington* doctrine applies to the MSA and related California statutes. Accordingly, the manufacturer defendants are immune from suit for their operation under the settlement agreement and implementing legislation.

The manufacturer defendants' motion to dismiss is GRANTED on this ground.

B. State action immunity

The manufacturer defendants also argue that this doctrine protects them from suit because the MSA and implementing legislation are state action. As discussed above, the Court agrees that the MSA and ***1104** enabling legislation are state action, approved

by state courts, enacted by the legislature, and enforced by state officials. Plaintiff argues that the MSA and these legislative enactments require *Midcal* analysis and that the MSA fails to meet the second *Midcal* requirement that the state "actively supervise" anticompetitive activity. Sanders also contends that the MSA is a "hybrid restraint" rather than direct state action.

Where there is direct state action affording immunity, the immunity extends equally to private parties and state actors. *See PTI,* 100 F. Supp.2d at 1196. The Court finds that the settlement itself, the Qualifying Act, and the Contraband Amendment are state action. Accordingly, both the manufacturer defendants and defendant Lockyer are immunized under the state action doctrine from antitrust liability for the MSA itself, the state's enactment of the Qualifying Act and Contraband Amendments, and their operation under the MSA regime.

Moreover, the MSA and related statutes are not hybrid restraints. A hybrid restraint is a government action delegating regulatory power to private parties so that they can enforce their own private market decisions. *Rice v. Norman Williams Co.,* 458 U.S. 654, 665, 102 S.Ct. 3294, 73 L.Ed.2d 1042 (1982) (Stevens, J., concurring); *Fisher v. City of Berkeley,* 475 U.S. 260, 268, 106 S.Ct. 1045, 89 L.Ed.2d 206 (1986); *324 Liquor Corp. v. Duffy,* 479 U.S. 335, 107 S.Ct. 720, 93 L.Ed.2d 667 (1987). The MSA does not authorize collusive action among the manufacturers or give them the regulatory authority to set prices in the cigarette market. It simply imposes unilateral payment obligations on OPMs and SPMs and escrow contributions

for NPMs. Without an agreement by the manufacturers to raise prices, which Sanders does not allege, these defendants would not be subject to antitrust liability even if the MSA were a hybrid restraint. *Miller v. Hedlund,* 813 F.2d 1344, 1351 n. 4 (9th Cir.1987) (private parties operating independently under a hybrid restraint are not liable under the Sherman Act).

The Third Circuit's discussion of *Parker* immunity for the manufacturers in *A.D. Bedell Wholesale Co. v. Philip Morris,* 263 F.3d 239, does not compel a contrary conclusion. In *Bedell,* the Court of Appeals affirmed the dismissal of claims brought against cigarette manufacturers on the basis of the *Noerr-Pennington* doctrine. Though it acknowledged that "[its] analysis could end [t]here," the *Bedell* court then applied *Midcal* analysis and concluded that the manufacturers were not entitled to *Parker* immunity because the "anticompetitive injury here resulted from the tobacco companies' conduct after implementation of the [MSA] and not from any further positive action by the states." 263 F.3d at 258. The Third Circuit also considered the MSA a hybrid restraint. *Id.* Because this Court concludes that the MSA is not a hybrid restraint, and because the Ninth Circuit's state action jurisprudence counsels a different finding, the *Bedell* court's apparent dicta on this subject is not persuasive.

Accordingly, the manufacturer defendants are entitled to state action immunity. Their motion to dismiss is GRANTED on this ground.

C. Immunity for state law claims

The manufacturer defendants also contend that state action immunity protects them from liability from plaintiff's state law claims as well. *Midcal* does not apply to the scope of state action immunity under state law. Instead of considering whether Congress intended to restrict state action under the Sherman Act, the Court must consider whether the state of California intended to restrict its own action ***1105** by enacting the MSA-related statutes. *See People v. City & County of San Francisco,* 92 Cal.App.3d 913, 917, 155 Cal.Rptr. 319; *Blank v. Kirwan,* 39 Cal.3d 311, 323, 216 Cal. Rptr. 718, 703 P.2d 58 (1985). Plaintiff does not address this argument in his opposition. The Court finds that the legislative acts of the state of California cannot violate the state's own antitrust law, and thus defendants are immune from liability for plaintiff's Cartwright Act, Unfair Competition Law, and common law unfair competition claims.

Consequently, the Court GRANTS defendants' motion to dismiss plaintiff's state law claims.

CONCLUSION

For the foregoing reasons and for good cause shown, the Court hereby GRANTS the motions to dismiss by defendant Lockyer and the manufacturing defendants. Plaintiff's complaint is dismissed with prejudice. [Docket #s 24, 25]

IT IS SO ORDERED.

No. 07-995

FILED
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OFFICE OF THE CLERK
SUPREME COURT, U.S.

IN THE

Supreme Court of the United States

STEVE SANDERS,
individually and as class representative,

Petitioner,

v.

EDMUND G. BROWN, in his official capacity as Attorney General of the State of California; PHILIP MORRIS USA INC.; R.J. REYNOLDS TOBACCO CO.; BROWN & WILLIAMSON TOBACCO CORP.; and LORILLARD TOBACCO CO.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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QUESTIONS PRESENTED

Petitioner invokes the Sherman Act to challenge the Master Settlement Agreement ("MSA")—a landmark settlement between 46 states and respondent tobacco companies—as well as related state statutes. These 46 states and every other party to the MSA agree that the MSA and those statutes do not authorize tobacco companies to fix prices or output or induce the companies to price their products in lockstep. The questions presented are:

1. Did the Court of Appeals correctly hold that the Sherman Act does not preempt the MSA-related state statutes because the statutes do not mandate or authorize conduct that is an antitrust violation?

2. Did the Court of Appeals correctly hold that respondent tobacco companies are immune from liability under the *Noerr-Pennington* doctrine when (as petitioner concedes) the companies enjoy such immunity for entering into the MSA and the complaint does not allege any other agreement in restraint of trade?

3. Did the Court of Appeals correctly hold that the State of California is immune from liability under the "state action" doctrine because the MSA and related statutes do not authorize any antitrust violation?

RULE 29.6 STATEMENT

Respondent Philip Morris USA Inc. is a subsidiary of Altria Group, Inc., which is the only publicly held company that owns 10% or more of Philip Morris USA Inc.'s stock.

All of the stock of Respondent R.J. Reynolds Tobacco Company is owned by R.J. Reynolds Tobacco Holdings, Inc., all of whose stock in turn is owned by Reynolds American Inc. Reynolds American Inc. is the only publicly held company that owns 10% or more of the stock of R.J. Reynolds Tobacco Holdings, Inc.

Respondent Brown & Williamson Tobacco Corporation (now known as Brown & Williamson Holdings, Inc.) ("Brown & Williamson") is wholly owned by BATUS Tobacco Services, Inc., which is a non-public holding company. Brown & Williamson's ultimate parent corporation is British American Tobacco, p.l.c., which is a publicly held United Kingdom corporation. All other indirect parent companies of Brown & Williamson are non-public companies.

Respondent Lorillard Tobacco Company is wholly owned by Lorillard, Inc., which is wholly owned by Loews Corporation. Shares of Loews Corporation are publicly traded. Loews Corporation has also issued Carolina Group stock, a publicly traded tracking stock. Other direct and indirect subsidiaries of Loews Corporation that are not wholly owned by Loews Corporation but have securities that are publicly traded are CNA Financial Corporation, Diamond Offshore Drilling, Inc., Boardwalk Pipeline Partners, LP, and Texas Gas Transmission, L.L.C.

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BRIEF IN OPPOSITION

INTRODUCTION[1]

Petitioner asks this Court to review the Court of Appeals' dismissal of his antitrust challenge to the Master Settlement Agreement ("MSA") and related California statutes. He contends that the circuits are split on three legal issues. But petitioner has concocted each purported conflict by misstating the holdings of the court below and its sister circuits. The Court of Appeals faithfully applied this Court's precedents and properly dismissed the complaint at the pleading stage. The petition presents no issue worthy of review.

As this Court has acknowledged, the MSA between 46 states and respondent tobacco companies (the "Manufacturers") is a "landmark agreement"—perhaps the most far-reaching and important government-induced settlement in history. *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525, 533 (2001). Courts in each of the settling states expressly approved it. Each settling state's legislature subsequently endorsed it by enacting implementing legislation. In light of "our national commitment to fed-

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[1] The petition is cited as "Pet." and the Appendix to the petition is cited as "App." Petitioner's briefs before the Court of Appeals are cited as "OB" and "CA9 Reply." The State of California's brief before the Court of Appeals and the amicus brief of the various Settling States are cited as "Cal. CA9 Br." and "Amici States CA Br." The Excerpts of Record before the Court of Appeals are cited as "ER" and the Clerk's Record is cited as "CR."

eralism," *City of Columbia v. Omni Outdoor Adver.*, 499 U.S. 365, 374 (1991), any one state's decision to enter the MSA and enact related laws is entitled to "'great respect.'" *Kelo v. City of New London*, 545 U.S. 469, 482 (2005) (citation omitted). When *46* states each make the independent judgment that the MSA is in the best interests of its citizens, the result is even more deserving of respect.

More than 20 lawsuits have been filed seeking to invalidate the MSA on antitrust grounds, and none has succeeded. Offering no new allegations or legal theories that would allow him to prevail where others have not, petitioner claims that the MSA has enabled the Manufacturers to charge supracompetitive prices for cigarettes. He asserts that the Sherman Act preempts the MSA and related statutes, and that the Manufacturers are liable for treble damages under California's antitrust law.

The District Court and a unanimous panel of the Court of Appeals held that petitioner's suit fails to state a claim as a matter of law. They held that: (1) the Sherman Act does not preempt the state laws petitioner challenges; (2) the Manufacturers are immune from liability under the *Noerr-Pennington* doctrine; and (3) the state is immune from liability under the *Parker* state-action doctrine.

Contrary to petitioner's assertion, there is no circuit split on whether the Sherman Act preempts the MSA or related legislation. With respect to the *Parker* and *Noerr-Pennington* immunity doctrines, petitioner similarly invents a circuit conflict by misstating the analyses and holdings of the Ninth Circuit and other courts.

To be sure, one circuit has taken a different *procedural* approach to dealing with a similar complaint in the early stages of the litigation. While the Ninth Circuit dismissed this case at the outset, the Second Circuit allowed a similar MSA challenge to proceed beyond the pleading stage. But this different procedural outcome is attributable to differences in the two courts' readings of the allegations of the complaints before them. The Second Circuit—in a decision rendered before this Court's ruling in *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955 (2007)—accepted the complaint's conclusory assertions that the MSA and related legislation authorized Sherman Act violations. *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, 225-26 (2d Cir. 2004). It thus allowed the plaintiffs *to try to prove facts* that might lead to preemption and defeat *Parker* immunity. *Id.* In contrast, the Ninth Circuit conducted a more critical examination of the complaint, including a review of the actual terms of the MSA (which was appended to the complaint), and reached a different conclusion. The Ninth Circuit's approach was correct, especially given *Twombly*'s emphasis on careful scrutiny of the complaint at the pleading stage.

This difference—wholly procedural, occurring in the early stage of litigation, and related to one particular contract—is simply not the sort of variance that warrants this Court's attention. Furthermore, any possible doubt on that issue is put to rest by the fact that *every* court that has examined the merits of the claim at issue here has reached the same conclusion: "The facts as proved . . . *tell a quite different story*" from the allegations of anticompetitive conduct in the plaintiffs' complaints. *Freedom Holdings, Inc. v. Spitzer*, 447 F. Supp. 2d 230, 248

(S.D.N.Y. 2004) (emphasis added), *aff'd*, 408 F.3d 112 (2d Cir. 2005); *see also infra* at 31 (collecting cases). The supposed "conflict" is thus no conflict at all; it amounts only to the question of when the antitrust challenge should be rejected: at the pleading stage, or after discovery.

The petition should be denied.

STATEMENT

The MSA and Implementing Legislation

Beginning in the mid-1990s, attorneys general in dozens of states filed lawsuits against the Manufacturers demanding reimbursement for smoking-related healthcare costs. App. A2-3. After prolonged litigation, a failed congressional solution, and months of negotiations, the Manufacturers and the states' attorneys general hammered out a comprehensive settlement. Attorneys general or governors representing 46 states, the District of Columbia, and five U.S. territories (the "Settling States" or "States") signed the MSA on behalf of their governments in 1998. App. A3-4. In each Settling State, the relevant court approved the MSA in a consent decree. App. A4. Each Settling State also enacted implementing legislation. App. A5.

Under the MSA, the Manufacturers paid billions of dollars to resolve claims of past harm. ER 87-88. Even more significantly, the MSA requires the Manufacturers to pay the States *billions more annually, in perpetuity*. App. A4. The MSA prescribes a formula for calculating the Manufacturers' annual payments. *Id.* The payment obligation increases or decreases depending on how many cigarettes a Manufacturer sells. App. A4-5. But regardless of how many cigarettes any Manufacturer sells,

each Manufacturer pays the same amount for each cigarette. *See* Amici States CA Br. 15-17.

The MSA also includes various terms governing the conduct of the Manufacturers—provisions that the Settling States have lauded as "significant measures designed to promote public health and prevent youth smoking." *Id.* at 2; *see id.* at 6 ("The MSA has had a dramatic positive impact on public health, and this will likely increase over time."). Among these measures are limits on the advertising, marketing, and promotion of tobacco products and the establishment of an independent national foundation to reduce youth smoking. ER 50-73.

The MSA invites any other cigarette manufacturer to sign on to the settlement. App. A4. Manufacturers that accept the invitation are known as "Subsequent Participating Manufacturers," or "SPMs," to distinguish them from the "Original Participating Manufacturers," or "OPMs." *Id.* SPMs agree to the various prospective reforms, including the obligation to pay a fixed per-cigarette cost, subject to an exemption: An SPM that signed the MSA within 90 days has no obligation to pay to the extent that its market share in a particular year is less than its 1998 market share (or 125% of its 1997 market share, if that is higher). *Id.* When an SPM crosses the volume threshold, it incurs a fixed per-cigarette cost for cigarettes sold above the threshold. ER 110-12.

Manufacturers that choose not to sign the MSA are obviously not bound by its terms. But in California, as in the other Settling States, these "Non-Participating Manufacturers," or "NPMs," do have obligations that are governed by state statute. App. B3; A5-6. The California Legislature enacted the

"Escrow Statute" (also called the "Qualifying Act"), which requires each NPM to contribute annually to an escrow fund based on the number of cigarettes it sells within the state. Cal. Health & Safety Code § 104557. The escrow fund is a security against future health-related costs for which an NPM might be held liable. App. A6. Thus, the fund can be used only to pay a settlement or a judgment against the NPM; whatever funds remain in escrow after 25 years revert to the NPM. *Id.*

The Escrow Statute prescribes precisely, on a per-cigarette basis, the NPMs' payment obligation. To strengthen enforcement of the Escrow Statutes, California and other states have enacted complementary legislation (petitioner calls it the "Contraband Amendment") providing that NPM-manufactured cigarettes may not be distributed unless the NPM is in compliance with the Escrow Statute. Cal. Bus. & Prof. Code § 22979; App. A6-7.

Neither the MSA nor the implementing legislation in any way limits each Manufacturer's freedom to set its own prices and output. Indeed, no provision in the MSA or the legislation purports to govern prices or output. And, because the payment obligations impose the same per-cigarette costs on all Manufacturers, they do not provide either an incentive to limit output or a disincentive to increase output. Finally, neither the MSA nor the legislation authorizes participants to enter into any agreement on prices or output.

Petitioner's Allegations and Legal Theory

Petitioner filed this lawsuit against the State of California and the Manufacturers under § 1 of the Sherman Act and California's antitrust law. Pur-

porting to represent all California smokers, petitioner seeks to invalidate what he calls the "anti-competitive provisions of the MSA" and the implementing legislation, ER 18, claiming they are preempted by the Sherman Act. He also seeks to recover billions of dollars from the Manufacturers for the alleged "supracompetitive prices" he claims the purported class was "forced to pay" as a result of the MSA. OB 10. Specifically, he alleges that the Manufacturers raised their prices more than twice the amount that would have been necessary to offset their MSA payment obligations. App. A7.

The essential element of a Sherman Act § 1 claim is a "contract, combination . . . or conspiracy, in restraint of trade." 15 U.S.C. § 1. But the *only* purportedly illegal agreement in restraint of trade alleged in the complaint is the MSA itself—and petitioner has conceded that he has no claim against the Manufacturers for negotiating and signing the MSA. App. B18; CR53 at 48-50.

Unable to point to any actionable agreement in restraint of trade, petitioner offers the theory that the MSA allows the Manufacturers to operate in a way that *resembles* a "horizontal output cartel," albeit without actually agreeing to raise prices or reduce output. *See* Pet. 12 (MSA "effectively" established a "horizontal output cartel"). Specifically, he alleges that the Manufacturers "have been able to raise prices with impunity and in lockstep." OB 10.

Petitioner's theory is based upon a misreading of the MSA, a contract to which he is not a party. He correctly notes that the MSA imposes increased payment obligations when a Manufacturer's market share increases. OB 22. From this he leaps to the counterfactual conclusion that these increased

payment obligations "offset or exceed[]" the increased revenue from any "market share gained through price competition," and thereby purportedly eliminate any incentive to cut prices. OB 10-11. Thus, according to petitioner, each Manufacturer has the "perfect incentive[]" to follow another's price hike, in order to avoid the purportedly negative effect of a market share increase. OB 17. Petitioner calls this theory his "key allegation," OB 25—and rightfully so, because without it his claim that the MSA creates something like an "output cartel" necessarily collapses.

The 46 States and every other party to the MSA, however, recognize that the express terms of the MSA flatly contradict petitioner's theory. Those terms make clear that the MSA and the related legislation require manufacturers to pay a flat per-cigarette cost for every cigarette they sell. This per-unit cost does not vary with market share. Thus, there is no reason for any manufacturer not to compete on price and gain market share. *See* Amici States CA Br. 17 ("[I]t is evident from the face of the MSA that there is no disincentive for any OPM to reduce prices or gain market share, [and] no output-limiting 'cartel.'").

Petitioner is *not* arguing that an agreement in restraint of trade should be inferred on the basis of the claimed lockstep pricing or other evidence. *See* App. A20. Nor could he. *See, e.g., Bell Atl. Corp. v. Twombly*, 127 S. Ct. 1955, 1964 (2007) (parallel conduct by itself is lawful and does not suggest conspiracy); *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 227 (1993) (describing parallel pricing in the tobacco industry as a "not . . . unlawful" consequence of oligopolistic interde-

pendence); *Williamson Oil Co. v. Philip Morris USA*, 346 F.3d 1287, 1299-1301 (11th Cir. 2003) (affirming grant of summary judgment in Sherman Act § 1 case against Manufacturers based on alleged lockstep pricing on ground that no reasonable jury could conclude that Manufacturers agreed to fix prices).

If petitioner's suit succeeded, he would void the MSA—with dramatic adverse effects on the States. He would cancel the flow of billions of dollars a year from the Manufacturers to the Settling States. He would also eliminate the far-reaching and unprecedented advertising and marketing restrictions.

The Legal Framework

Respondents moved to dismiss on the grounds that petitioner failed to plead a preemption claim and that their conduct was immune from liability under the *Noerr-Pennington* doctrine and *Parker* state action doctrine. All parties agree on the basic legal framework on all three issues—as did the District Court, the Court of Appeals, and the two circuits petitioner invokes in attempting to raise a conflict.

1. Preemption. A state statute "is not preempted by the federal antitrust laws simply because the state scheme might have an anticompetitive effect." *Rice v. Norman Williams Co.*, 458 U.S. 654, 659 (1982); *accord Fisher v. City of Berkeley*, 475 U.S. 260, 264 (1986). Because the "function of government may often be to tamper with free markets," the circumstances under which the federal antitrust laws will preempt a state statute are narrowly circumscribed. *Fisher*, 475 U.S. at 264; *see Exxon Corp. v. Governor of Md.*, 437 U.S. 117, 133 (1978)

("[I]f an adverse effect on competition were . . . enough to render a state statute invalid, the States' power to engage in economic regulation would be effectively destroyed.").

"A party may successfully enjoin the enforcement of a state statute *only* if the statute on its face *irreconcilably conflicts* with federal antitrust policy." *Rice*, 458 U.S. at 659 (emphasis added). Such an irreconcilable conflict will occur only when the state law

> mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute. Such condemnation will follow under § 1 of the Sherman Act when the conduct contemplated by the statute is in all cases a *per se* violation.

Id. at 661; *accord Fisher*, 475 U.S. at 265; Pet. 15-16.

2. *Parker* immunity. The state action immunity doctrine described in *Parker v. Brown*, 317 U.S. 341 (1943), mirrors the foregoing preemption principles. For reasons of "federalism and state sovereignty," *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 343 (1987), the basic rule is that the Sherman Act does not apply to "state action or official action directed by a state." *Parker*, 317 U.S. at 351. "In a dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not

lightly to be attributed to Congress." *Parker*, 317 U.S. at 351. And if a state action enjoys *Parker* immunity, then so do the "regulated private parties" who operate under the law. *Southern Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48, 56-57 (1985).

Just as there is a single exception to the rule against Sherman Act preemption of state action, there is a single exception to the rule in favor of state action immunity from the Sherman Act: A state cannot "give immunity to [private parties] who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Parker*, 317 U.S. at 351. Sherman Act violations authorized by a state can come in the form of a private restraint (which petitioner does not allege) or a so-called "hybrid restraint" (which petitioner does allege).

The classic private restraint is the one this Court encountered in *FTC v. Ticor Title Insurance Co.*, where the state authorized title insurance companies to enter into a "private pricefixing arrangement[]" among themselves. 504 U.S. 621, 633 (1992). This Court held that the title companies could not claim immunity for their per se violation of the Sherman Act, even though state law authorized their conduct. *Id.* at 639-40.

A state creates a hybrid restraint when it grants a private party "a degree of private regulatory power" that allows that party to compel other private actors to follow its pricing or other "private marketing decisions." *Fisher*, 475 U.S. at 268 (internal quotation marks omitted); *accord 324 Liquor*, 479 U.S. at 345 n.8. For example, in *324 Liquor*, a state statute authorized alcohol wholesalers

to dictate the prices charged by retailers; the penalty for a retailer's non-compliance was a fine and loss of its license. 479 U.S. at 340. The Court held that the Sherman Act preempted the statute because it created a hybrid restraint that constituted resale price maintenance in violation of Sherman Act § 1. *Id.* at 343-45 & n.8.

A statute or other state action that authorizes or compels per se Sherman Act violations (such as the private restraint in *Ticor* or the hybrid restraint in *324 Liquor*) is a necessary precondition to establishing the inapplicability of *Parker* immunity, but is not by itself sufficient. The Court in *Midcal* held that even a statute or other state action authorizing per se Sherman Act violations will be entitled to *Parker* immunity, if the restraint is (1) "actively supervised" by the state and (2) "clearly articulated and affirmatively expressed as state policy." *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980); *see Ticor*, 504 U.S. at 633. Similarly, a statute that would otherwise be preempted by the Sherman Act can be saved if the state satisfies the *Midcal* requirements. *Fisher*, 475 U.S. at 265.

Because petitioner does not allege a private restraint (i.e., petitioner "does not allege that the tobacco companies have agreed amongst themselves to fix prices," App. A8), his sole argument for preemption, and against *Parker* immunity, is that the cartel-like results that the MSA supposedly induces amount to a hybrid restraint. Thus, if the MSA regime does *not* grant the Manufacturers private regulatory power that allows them to legally compel other private parties to follow their pricing or marketing decisions (i.e., does not create a hybrid re-

straint), it will be protected by *Parker*, and will not be preempted, without the need to inquire whether it satisfies the *Midcal* requirements.

3. *Noerr-Pennington* immunity. *Noerr-Pennington* immunity derives in part from the recognition that laws intended to govern competition in commercial markets "are not at all appropriate for application in the political arena." *Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 141 (1961); *see also United Mine Workers v. Pennington*, 381 U.S. 657, 669-70 (1965). Rooted also in First Amendment principles, the doctrine holds that businesses must be free to "use the channels and procedures of state and federal agencies and courts to advocate their causes and points of view respecting resolution of their business and economic interests *vis-à-vis* their competitors," and the antitrust laws cannot be used to penalize them for their advocacy. *Cal. Motor Transp. Co. v. Trucking Unlimited*, 404 U.S. 508, 510-11 (1972); *Noerr*, 365 U.S. at 137-38. The immunity applies even if the "sole purpose" of a party's conduct is to restrain trade or destroy competitors. *Noerr*, 365 U.S. at 138-40.

Courts have uniformly held that *Noerr-Pennington* protects private parties that enter into litigation settlements with the government, and petitioner has conceded from the start that the Manufacturers enjoy *Noerr-Pennington* immunity for negotiating and entering into the MSA. App. A16; B18-19; CR53 at 48-50.

The District Court Dismisses the Complaint and the Court of Appeals Affirms

Applying these settled principles, the District Court granted the motions to dismiss filed by the State of California and the Manufacturers. The District Court held that the Sherman Act does not preempt the implementing statutes, App. B14-16; that petitioner failed to plead a claim that could defeat *Parker* immunity, App. B9-14, 20-22; and that petitioner failed to plead a claim that could survive *Noerr-Pennington* immunity, App. B16-20.

A panel of the Ninth Circuit unanimously affirmed the dismissal. Central to the Court of Appeals' analysis was the decision to go behind the allegations and "analyze the MSA"—which was attached to the complaint and was "obviously central to the claim," App. A11—and evaluate whether petitioner's allegations about the MSA's effect bore any relation to what the MSA actually says.

1. Preemption. The Court of Appeals held that the implementing legislation is not preempted, because it is not in "'irreconcilable' conflict" with federal law. App. A12 (quoting *Rice*, 458 U.S. at 659). The court explained that neither of the statutes plaintiff challenges "explicitly allow[s] price fixing, market division, or other *per se* illegal monopolistic behavior." *Id.*

The Court of Appeals rejected petitioner's argument that the statutes "create such high barriers to NPMs' market entry and ability to price-compete that they have 'virtually guaranteed collusion and monopoly prices.'" App. A12-13 (citation omitted). It explained that the actual terms of the MSA—as distinguished from petitioner's characterization of

them—conclusively show that there is nothing to stop any competitor from entering the market and undercutting the MSA's participants on price. App. A13. Although "[t]he statutes . . . may cause higher prices," the court said,

> [n]othing . . . forces the NPMs to either peg their prices to those of participating manufacturers, or to refrain altogether from entering the market. If the OPMs really are charging artificially high prices, and thus making artificially high profits, an NPM conceivably could compete on price by charging a "normal" price and still make a "normal" profit, even taking the escrow payment into account.

Id.

2. *Parker* immunity. The Court of Appeals held that because the state did not authorize any per se violations of the Sherman Act, "*Parker* immunity protects the state from antitrust liability for entering into the MSA and for passing the implementing statutes." App. A28.

The court rejected petitioner's theory that the MSA and the implementing legislation create a hybrid restraint. App. A29. The Court of Appeals explained that under this Court's precedent the distinguishing feature of a hybrid restraint is a "state's decision to let producers dictate market conditions to others." *Id.* Since "the MSA involves no such delegation of *per se* illegal power such as the ability to fix prices," the court "conclude[d] that the MSA cannot be classified as a hybrid restraint." App. A30.

Accordingly, the court held that the state was not required to engage in active supervision of cigarette prices to obtain immunity, because "the *Midcal* test does not apply to sovereign state acts, which are immune from antitrust liability so long as they" do not "authoriz[e] *per se* illegal activities" by private parties. App. A27.

3. *Noerr-Pennington* immunity. The Court of Appeals also held that the Manufacturers are shielded by *Noerr-Pennington* immunity. App. A15-21.

The court began with the observation that "*Noerr-Pennington* immunity protects private parties from liability for negotiating and entering into settlements or other agreements with the government," App. A16—a point petitioner had conceded, App. B18. The court then rejected petitioner's argument that "even if *Noerr-Pennington* immunity protects the defendants from liability for the MSA itself, it does not protect the tobacco defendants from liability for increasing prices after the MSA." App. A18. The court acknowledged that the *Noerr-Pennington* doctrine does not necessarily immunize *all* conduct the Manufacturers might have engaged in after the MSA; if, for example, the Manufacturers had made post-MSA "agreements . . . to engage in the operation of an output cartel," such agreements "might not be immune from liability" under *Noerr-Pennington*. App. A20 (internal quotation marks omitted). But that possibility was beside the point, the court held, because petitioner's complaint "*does not allege any such subsequent agreement in restraint of trade.*" *Id.* (emphasis added). Thus, because the only agreement to restrain trade alleged in the complaint is the MSA itself—and entry into

the MSA is immunized by *Noerr-Pennington*—the court concluded that the complaint states no claim against the Manufacturers. App. A21.

In the end, the court held, "because [petitioner's] complaint is based on injuries caused directly by government action"—and not based on post-MSA activities that would themselves be antitrust violations—"*Noerr-Pennington* immunity shields the tobacco defendants from liability for the alleged supracompetitive price increases." App. A20-21 (citing *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 499 (1988)).

REASONS FOR DENYING THE PETITION

The petition should be denied because: (i) it presents no actual circuit conflict; (ii) this case presents no issue of national importance that warrants this Court's intervention; and (iii) the Court of Appeals' analysis was both correct and consistent with this Court's established jurisprudence.

I. THERE IS NO CIRCUIT CONFLICT ON ANY OF THE QUESTIONS PRESENTED.

Petitioner asserts a trio of circuit conflicts wrapped up in one case. In truth, there is no conflict on any of the three questions petitioner presents. The various circuits agree on the basic legal principles. *See supra* at 9-13. At most, they differ on how to assess allegations regarding the MSA at the pleading stage—a case-specific application of settled law that does not merit this Court's attention. *See* Sup. Ct. R. 10.

In fact, on at least three previous occasions, this Court has denied certiorari in MSA cases involving similar antitrust challenges in a similar posture.

See Mariana v. Fisher, 338 F.3d 189 (3d Cir. 2003), *cert. denied*, 540 U.S. 1179 (2004); *A.D. Bedell Wholesale Co. v. Philip Morris Inc.*, 263 F.3d 239 (3d Cir. 2001), *cert. denied*, 534 U.S. 1081 (2002); *Hise v. Philip Morris Inc.*, 208 F.3d 226 (10th Cir.), *cert. denied*, 531 U.S. 959 (2000). This Court's intervention is even more unwarranted now. In light of subsequent developments, described below, the two courts of appeals on the other side of the claimed conflict would likely assess the complaint allegations about the MSA as the Court of Appeals did here, if confronted with a motion to dismiss today.

A. There Is No Circuit Conflict on Whether the Sherman Act Preempts the MSA.

Petitioner does not assert that any court of appeals has rejected the preemption principles set forth above. *See supra* at 9-10. Indeed, each court recited exactly the same preemption principles, starting with the baseline rule that the Sherman Act does not preempt a state statute unless the "conduct contemplated by the statute [is] 'in all cases a per se violation' of the federal antitrust laws." *Compare Freedom Holdings*, 357 F.3d at 223 (quoting *Rice*, 458 U.S. at 661), *with Tritent Int'l Corp. v. Kentucky*, 467 F.3d 547, 554 (6th Cir. 2006) (same), *and* App. A12 (same).

Rather than claiming a disagreement over basic antitrust principles, petitioner focuses on an application of these settled principles to a specific—indeed, unique—context. He asserts that "[t]he decision below expands an existing split . . . over whether the MSA and its related statutes are preempted by federal antitrust law," because "[t]he

Second Circuit . . . has held that . . . the [implementing] statutes are preempted." Pet. 20-21. He is wrong. No circuit—indeed, no court at any level—has ever so held.

The Second Circuit case petitioner invokes is *Freedom Holdings*. There, the plaintiffs sued New York State, seeking to enjoin its implementing legislation on preemption grounds. 357 F.3d at 208-09. Addressing the allegations at the pleading stage, the Second Circuit held only that the plaintiffs had "sufficiently *alleged* a *per se* violation of the Sherman Act," *id.* at 226 (emphasis added), which meant only that *if "the allegations of the Complaint [were] proven,"* they would have a claim for preemption, *id.* at 232 (emphasis added). That holding rested entirely on the court's assumption, for purposes of the motion to dismiss, that the complaint was accurate in alleging that the MSA's payment obligations effectively penalized Manufacturers for increasing output, and therefore gave rise to market behavior that resembled an output cartel. *Id.* at 225-26.

That is not the same as a holding that "the statutes *are* preempted." Pet. 20-21 (emphasis added). Subsequent proceedings in the case underscore just how inaccurate that description is. On remand, the plaintiffs sought a preliminary injunction against enforcement of the same implementing legislation that petitioner challenges here. *Freedom Holdings, Inc. v. Spitzer*, 447 F. Supp. 2d 230, 248 (S.D.N.Y. 2004), *aff'd*, 408 F.3d 112 (2d Cir. 2005). The district court noted that the Second Circuit's holding was "based, not on fact, but on plaintiffs' allegations of fact that they claim to be able to prove. *The facts as proved, however, tell a quite different story.*" *Id.* (emphasis added).

The district court found that the complaint's allegations about the effects of the MSA were inconsistent with the MSA's express terms. It noted that the payment obligations of NPMs "are essentially a flat tax, assessed at a flat rate per cigarette sold" and that this does not prevent price competition among cigarette manufacturers. *Id.* at 258. For this reason, the court observed that, "contrary to plaintiffs' allegations, [NPMs'] incremental costs do not rise with their volume of sales, and they are not in any manner obliged to increase their prices in lockstep with the OPMs." *Id.* at 261; *see also Grand River Enters. Six Nations Ltd. v. Pryor*, No. 02-5068, 2006 WL 1517603 at *8-*9 (S.D.N.Y. May 31, 2006) (finding no likelihood of success on claim that MSA implementing statutes are preempted by Sherman Act and denying preliminary injunction), *aff'd on other grounds*, 481 F.3d 60 (2d Cir. 2007).

To be sure, the court below and the Sixth Circuit (in *Tritent*) rejected at the pleading stage complaints similar to the one the Second Circuit allowed to proceed beyond the pleading stage. But the difference was not (as petitioner asserts) about the ultimate question of the "validity of the MSA and its implementing legislation." Pet. 21. As the Sixth Circuit pointed out, the Second Circuit simply accepted as true the complaint's conclusory, and inaccurate, allegations concerning the MSA's operation. *See Tritent*, 467 F.3d at 557; Amici States CA Br. 22-24 & n.6. By contrast, the Ninth and Sixth Circuits scrutinized the MSA more closely, under the rule that "a court can consider a document on which the complaint relies if the document is central to the plaintiff's claim." App. A11.

If a court of appeals ever holds that the MSA and implementing statutes *are* preempted, that might well create a circuit conflict worthy of this Court's attention. At a minimum, this Court should await the Second Circuit's review of the district court's ruling on remand in *Freedom Holdings*. If the Second Circuit were to hold that the MSA regime is actually preempted, the Court would at that point have a basis for determining whether an actual, meaningful conflict exists. But without such a hypothetical ruling, the different outcomes in these cases boil down to the procedural question of how rigorously a court should scrutinize a complaint's allegations concerning a unique contract. That is not the sort of disagreement that is worthy of this Court's attention.

Indeed, the issue is particularly unworthy of review because there is good reason to believe the Second Circuit would not reach the same result today in light of this Court's recent guidance in *Twombly*. There, this Court reversed the Second Circuit in an antitrust case for sustaining a complaint when the claim was merely "conceivable," but not "plausible." 127 S. Ct. at 1974. *Twombly* directed the lower courts to do exactly what the Ninth Circuit did here: carefully scrutinize the complaint "for enough fact to raise a reasonable expectation that discovery will reveal evidence" that the plaintiff's allegations will be borne out. *Id.* at 1965. This Court directed the lower courts to take notice of "the full contents" of published documents "referenced in the complaint," *id.* at 1972 n.13, and assess allegations of the complaint "in light of common economic experience," *id.* at 1971, just as the Ninth Circuit did here.

B. There Is No Circuit Conflict on *Parker* Immunity.

Petitioner also asserts that there is a circuit split on "whether a state scheme, enabling private antitrust violations, that fails the *Midcal* test nonetheless receives *Parker* immunity." Pet. 25. No such split exists, because the Ninth Circuit did not hold that a state scheme "enabling private antitrust violations" receives *Parker* immunity even if it fails the *Midcal* test. Instead, the court held that the MSA and related statutes are entitled to *Parker* immunity precisely because they do *not* enable private antitrust violations. As the Ninth Circuit put it: "The MSA and the implementing statutes authorize no illegal activity .... We therefore hold that *Parker* immunity protects the state from antitrust liability ...." App. A28. Far from creating a circuit split, the Ninth Circuit's view of the law is precisely the same as the Second's and Third's: If the state action authorizes violations of the Sherman Act, *Parker* immunity is available only if the state can satisfy the *Midcal* requirements of active supervision and clear articulation. *See Freedom Holdings*, 357 F.3d at 226; *Bedell*, 263 F.3d at 255.

Petitioner is also wrong when he asserts that "the Second and Third Circuits ... held that the MSA and those statutes *failed* the *Midcal* test and thus were not entitled to *Parker* immunity." Pet. 25 (emphasis in original). This assertion is wrong for the same reason that petitioner's similar statement about preemption is wrong: Both cases were pleading cases, and thus the courts could not possibly

have held on the merits that the statutes "were not entitled to *Parker* immunity."[2]

There is an additional reason why any disagreement on this pleading matter is inconsequential: The Third Circuit ultimately reached the same result as the Ninth Circuit here, only on the basis of a different brand of immunity. In *Bedell*, the Third Circuit *dismissed* the antitrust complaint against the Manufacturers (the only defendants there) on *Noerr-Pennington* grounds—just as the Ninth Circuit did in this case. 263 F.3d at 250-54. In a subsequent case, the Third Circuit extended that holding to state officers (the only defendants in that case). *See Mariana*, 338 F.3d at 197-200. Thus, if this case had been filed in the Third Circuit, it not only would have been dismissed at the pleading stage, but it would have been dismissed on the ground that both the state and the Manufacturers were immune from suit. That is what the Ninth Circuit did here.[3]

---

[2] In this case, the Ninth Circuit observed, imprecisely, that "[t]he Second Circuit in *Freedom Holdings* and the Third Circuit in *Bedell* applied the *Midcal* analysis and held that *Parker* immunity does not protect the state from liability for entering into the MSA." App. A28-29. The court obviously did not mean to say that the other courts had reached that ultimate merits conclusion, when all they had before them was the question whether the complaint stated a claim.

[3] In *Bedell*, after holding that *Noerr-Pennington* barred the complaint and that "our analysis could end here," 263 F.3d at 254, the Third Circuit went on to state that based on the complaint allegations, "defendants are not immune under the *Parker* immunity doctrine." *Id.* at 266. Although the Third Circuit has characterized this statement as a "holding," it plainly was not, because it was not necessary to the dispo-

(footnote continued...)

C. There Is No Circuit Conflict on *Noerr-Pennington* Immunity.

Every court that has addressed the issue—including the Third Circuit in *Bedell*, 263 F.3d at 250-54—has held, on the pleadings, that the *Noerr-Pennington* doctrine immunizes the Manufacturers from liability in an antitrust suit challenging the MSA.[4] Nevertheless, petitioner incorrectly insists there is a conflict between the Ninth Circuit and the Second Circuit on two *Noerr-Pennington* issues.

Petitioner's main argument is that "the Ninth Circuit [held], in conflict with the Second Circuit, that the *Noerr-Pennington* doctrine applies not only to protect petitioning activity, but also to immunize any resulting anticompetitive legislation . . . undertaken pursuant thereto." Pet. i; *see* Pet. 24. But the Ninth Circuit did not hold any such thing. To the contrary, it noted that "defendants here *do not claim* that *Noerr-Pennington* immunity protects *the implementing statutes* from preemption," and accordingly never decided the issue. App. A21 n.9

(continued from previous page)
sition of the case—indeed, it flatly contradicts that disposition. *Mariana*, 338 F.3d at 204 ("Critics may with some justification regard our discussion of *Parker* immunity as dictum, and well it may be."). In any event, the Third Circuit itself has since questioned the soundness of its *Parker* analysis. *Id.* at 203.

[4] *See* App. A15-21, *aff'g* App. B18-20; *Bedell*, 263 F.3d at 250-54, *aff'g* 104 F. Supp. 2d 501, 505-07 (W.D. Pa. 2000); *Hise*, 208 F.3d 226, *aff'g* 46 F. Supp. 2d 1201, 1205-07 (N.D. Okla. 1999); *PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179, 1191-97 (C.D. Cal. 2000); *Forces Action Project LLC v. California*, No. 99-0607 (N.D. Cal. filed Jan. 16, 2002).

(emphasis added). The Ninth Circuit even quoted the Second Circuit's view that "the immunity for advocacy cannot sensibly protect the resultant anticompetitive legislation from being held to be preempted," *id.* (quoting *Freedom Holdings*, 357 F.3d at 233), and observed that it "may be correct." *Id.*

Petitioner also asserts a conflict, again between the Ninth Circuit and the Second Circuit, over whether *Noerr-Pennington* immunizes private "conduct undertaken pursuant" to such "anticompetitive legislation." Pet. i. But there is no circuit split with respect to this question either. Contrary to petitioner's assertion, the Second Circuit did not decide whether, or under what circumstances, "*Noerr-Pennington* immunity . . . reach[es] subsequent . . . conduct" of a private actor operating under the state legislation. Pet. 24. The Second Circuit had no occasion to decide the issue because there *were* no private parties in *Freedom Holdings*; it was a lawsuit against the state alone. As the Second Circuit noted, "Here, [the plaintiffs] *do not seek to impose liability on private defendants* but rather seek to have the Contraband Statutes declared invalid." 357 F.3d at 233 (emphasis added).

Moreover, granting certiorari on this question would be pointless, because the outcome of this case would be the same regardless of the answer. As the Ninth Circuit pointed out, the Manufacturers cannot be held liable for post-MSA conduct because *Noerr-Pennington* immunizes their entry into the MSA and petitioner does not allege any other agreement in restraint of trade. App. A20-21.

II. THIS PLEADING CASE RAISES NO ISSUE OF NATIONAL IMPORTANCE.

Petitioner argues that his petition raises concerns "of national importance" for three reasons. Pet. 27-32. While there is no doubt about the importance of the *MSA*, petitioner is wrong about the importance of the issues presented at this early juncture.

1. Petitioner's main claim of importance is that this case presents an "intractable division among the courts of appeals on the validity of the MSA and its implementing legislation." Pet. 21; *see* Pet. 29 (noting "inherent importance of the legality of the MSA"). But as we have demonstrated above, there is no such division. No court—district court or court of appeals—has held the MSA or implementing legislation invalid.

Petitioner conflates the willingness of plaintiffs' lawyers to roll the dice by filing new lawsuits challenging the MSA with "[t]he continuing unsettled legality of the MSA's funding mechanisms." Pet. 28. As this Court recently observed, the willingness of plaintiffs' lawyers to bring "even anemic cases" in hopes of extracting a settlement or hitting a jackpot is a problem to be addressed, as the Court of Appeals did here, by carefully scrutinizing pleadings. *Twombly*, 127 S. Ct. at 1967. It is not a basis to rush "anemic cases" to this Court.

In any event, other lawsuits unsuccessfully challenging the MSA and implementing legislation on antitrust grounds are currently pending before the courts of appeals. *See Xcaliber Int'l Ltd., LLC v. Edmondson*, No. 04-0922, 2005 WL 5654220 (N.D. Okla. May 20, 2005), *appeals docketed,* No. 05-

5175 (10th Cir. Sept. 29, 2005) & No. 05-5178 (10th Cir. Oct. 3, 2005); *Xcaliber Int'l Ltd., LLC v. Kline*, No. 05-2261, 2006 WL 288705 (D. Kan. Feb. 7, 2006), *appeal docketed*, No. 06-3061 (10th Cir. Feb. 16, 2006); *Grand River Enters. Six Nations Ltd. v. Beebe*, 418 F. Supp. 2d 1082 (W.D. Ark. 2006), *appeal docketed*, No. 08-1436 (8th Cir. Feb. 26, 2008). Unlike this case, two of those cases (*Edmondson* and *Kline*) went up on appeal after full discovery and grants of summary judgment to the defendants. If a circuit conflict ever developed, and this Court were interested in deciding the ultimate question whether the Sherman Act preempts the MSA, cases in that posture would be better vehicles than this case.

2. Next, petitioner posits that "the questions presented here are of general importance to the proper implementation of antitrust law generally." Pet. 29-30. Specifically, he claims that the Court of Appeals "reached a holding that essentially renders [*Midcal*] a dead letter in most circumstance[s]." Pet. 30. Petitioner portrays the Court of Appeals' opinion as holding that a state law is always immune—and need not satisfy the *Midcal* requirements—even if it authorizes antitrust violations. *Id.* But as we have already demonstrated, the Court of Appeals held no such thing. It expressly recognized that *Midcal*'s requirements *must* be met when "a state law . . . attempts to 'give immunity to those who violate the Sherman Act by authorizing them to violate it.'" App. A21-22, 28 (citation omitted). Thus, far from purporting to "overrule[]" *Midcal*, Pet. 30, as petitioner charges, the Court of Appeals was entirely faithful to the decision.

Petitioner also asserts that "the continued uncertainty as to the validity of *Midcal* and its relationship to [*Hoover v. Ronwin*, 466 U.S. 558 (1984)], has been a source of confusion in the lower courts for many years." Pet. 30-31. If the lower courts really were confused, one would have expected petitioner to adduce a long string cite of cases expressing confusion. There is no string cite, because there is no confusion.

In *Hoover*, the Court held that the state action there in issue—a state's decision about who should be admitted to practice law in Arizona—was a sovereign act of the state. 466 U.S. at 570-74. Because the state did not authorize private parties to violate the Sherman Act—it did not, for example, let a group of private practitioners dictate which of their competitors should be admitted to practice law—it was immune under *Parker*, without any need to satisfy the *Midcal* requirements. *Id.* at 575. Thus, there is no tension or inconsistency between the two decisions; *Hoover* simply involved a particular set of facts in which it was unnecessary to apply the *Midcal* requirements to conclude that immunity was available. *See Mass. Food Ass'n. v. Mass. Alcoholic Beverages Control Comm'n*, 197 F.3d 560, 563-66 (1st Cir. 1999) ("What is centrally forbidden is state licensing of arrangements between private parties that suppress competition—not state directives that *by themselves* limit or reduce competition." (emphasis in original)), *cert. denied*, 529 U.S. 1105 (2000).

3. Finally, petitioner asserts that *Parker* immunity should not apply because when many states—rather than just one—take similar action, the federalism concerns that animate *Parker* evaporate. Pet.

31. Petitioner has it exactly backwards. If only one State had decided that the MSA's terms were in the best interests of its citizens, the courts would owe that judgment "special deference . . . in our system of federalism." *Youngblood v. West Virginia*, 547 U.S. 867, 874 (2006). When *46* States each make the same independent judgment, the respect is amplified, not muted. *Cf. New York v. O'Neill*, 359 U.S. 1, 6 (1959) (uniform laws adopted by 42 states "increas[es] harmony within the federalism created by the Constitution").

The assertion that the MSA "encroaches upon national authority over a national market," Pet. 31, is equally meritless. As the Fourth Circuit has held, the MSA "does not increase the power of the States at the expense of federal supremacy and . . . , therefore, it is not an interstate compact requiring congressional approval under the Compact Clause." *Star Scientific Inc. v. Beales*, 278 F.3d 339, 360 (4th Cir.), *cert. denied*, 537 U.S. 818 (2002); *see id.* ("[T]he [MSA] 'does not purport to authorize the member States to exercise any powers they could not exercise in its absence.'" (citation omitted)). Petitioner's failure here even to assert a Compact Clause claim shows that not even he is persuaded by his "encroachment" argument. In any event, Congress has recognized and endorsed the MSA by authorizing each Settling State to use MSA payments for any expenditures determined appropriate by the State. 42 U.S.C. § 1396b(d)(3)(B).

III. THE COURT OF APPEALS' ANALYSIS IS CORRECT AND FAITHFULLY APPLIES THIS COURT'S PRECEDENTS.

Petitioner asserts that the Court of Appeals' opinion is "wrong" and in "direct conflict" with decisions of this Court. Pet. 32. But petitioner fails to identify any such conflict. And each claim of error is meritless.

1. Petitioner asserts that the Court of Appeals "erroneously applied the standards for a pre-implementation facial challenge" to an "as-applied post-implementation challenge" to the MSA regime. *Id.* But as petitioner made clear in his complaint, and as the Court of Appeals recognized, he is seeking relief on the ground that the implementing statutes are "*facially void* as a *per se* restraint of trade." ER 17 (emphasis added); App. A10 n.6 (same).

In any event, the standard petitioner says the court *should* have applied—considering the "'economic realities of the relevant transactions'"—is the standard the court did in fact apply. Pet. 33 (citation omitted). Examining the MSA itself, the Court held that, contrary to the complaint's allegations, "[n]othing . . . forces the NPMs to either peg their prices to those of participating manufacturers, or to refrain altogether from entering the market." App. A13.

Petitioner, a complete stranger to the contract, offers his own idiosyncratic interpretation of the MSA, insisting that when the MSA calculates the Manufacturers' payment obligations, it punishes them for increasing their market share. *See* Pet. 9-11. But the States that are the actual parties to the MSA reject his interpretation, describing it as "a

fundamental misreading of the MSA and Escrow Statutes." Amici States CA Br. 13 (joined by 41 states, D.C., and three territories); *see id.* at 14-17; Cal. CA9 Br. 9-11. Every court that has addressed this issue on the merits agrees with the parties to the MSA. *Grand River*, 2006 WL 1517603, at *9 ("The MSA does not create disincentives for OPMs, SPMs or NPMs to restrict output or to avoid reducing prices."); *Xcaliber Int'l*, 2005 WL 5654220, at *5 ("[T]here is no evidence that the MSA incorporates penalties for increased market share by any class of PM which would serve to effect a market-sharing or price-fixing agreement."); *Freedom Holdings*, 447 F. Supp. 2d at 261 (NPMs' "incremental costs do not rise with their volume of sales, and they are not in any manner obliged to increase their prices in lock-step with the OPMs.").

As these courts and the parties to the MSA recognize, the MSA imposes a set unit cost on every cigarette that remains the same regardless of how many cigarettes a manufacturer sells. It is indisputable that this type of payment mechanism does *not* eliminate the incentive to cut prices or increase market share. Indeed, even petitioner and the Second Circuit agree with this proposition. CR53 at 42; *see Freedom Holdings*, 357 F.3d at 229 (a fixed per-cigarette cost "would not prevent price competition"). Thus, the linchpin of petitioner's output cartel/hybrid restraint theory—that the payment obligations encourage lockstep pricing by creating a disincentive to compete on price—is belied by the "economic realities" of the MSA's own terms.

2. Petitioner also asserts, without citation to any authority, that the Court of Appeals erred in concluding that the MSA and related statutes do not

create a hybrid restraint. Pet. 33. Petitioner is wrong. This Court has made clear that such a restraint arises *only* when the government *delegates* to a private actor "'a degree of private regulatory power'" that enables it to mandate compliance by other private actors with its "private marketing decisions" by force of law. *Fisher*, 475 U.S. at 268 (quoting *Rice*, 458 U.S. at 666 n.1 (Stevens, J., concurring)); *accord 324 Liquor*, 479 U.S. at 345 n.8 (citing *Fisher*); *Midcal*, 445 U.S. at 103. Thus, each arrangement that this Court has labeled a hybrid restraint has involved a situation in which private actors are *legally compelled* to charge the prices established by another private actor. *See 324 Liquor*, 479 U.S. at 340; *Midcal*, 445 U.S. at 100; *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384, 386-87 (1951). Indeed, petitioner acknowledged below that "legal compulsion . . . is the hallmark of a hybrid restraint." CA9 Reply 17.

The Court of Appeals correctly held that no hybrid restraint is involved here. The state has not delegated any regulatory authority to the Manufacturers. App. A30. Each company sets its own prices and has *no* power to set the prices or control the output of others, much less any such power backed by the state.

Rather than challenge that conclusion, petitioner shifts ground and asserts a novel definition of a hybrid restraint: "[T]he MSA and the related statutes were not simply unilateral state action, they were the result of an *agreement* with and among the major tobacco companies, which agreement effectively coerced state legislatures to adopt the statutes provided for in the MSA." Pet. 33. Without citation to any authority from this Court, petitioner calls

this "a classic instance of a hybrid restraint rather than unilateral regulation." *Id.*

But this Court has never suggested that the definition of hybrid restraint has anything to do with whether the state arrived at its policy choices through negotiation with private interests or whether state legislation was the product of careful deliberation or "effective[] coerc[ion]"—whatever that means. *See id.* That is presumably why petitioner never offered his novel definition of hybrid restraint in the lower courts.

Petitioner's suggestion that the MSA regime should be treated as a hybrid restraint simply because "the states left the OPMs free to make marketing decisions regarding price increases without supervision" is also wrong. *Id.* Under *Parker* and *Midcal*, economic actors *are* free to make such decisions without state supervision, *unless* the state has authorized those actors to engage in antitrust violations. Where, as here, the state has *not* authorized private parties to violate the antitrust laws, the *Parker* doctrine permits states to regulate conduct without the need for "active supervision."

3. Petitioner next argues that there can be no *Parker* immunity because the MSA is not a sovereign state act. According to petitioner, only "legislative" conduct may be considered sovereign state action. Pet. 34-35. Petitioner does not explain why *Parker* immunity should not apply to the executive branch. This Court has never held that it does not, and every court of appeals to consider the question has agreed with the Ninth Circuit that the immunity covers the actions of executive-branch officials. *See Neo Gen Screening, Inc. v. New England Newborn Screening Program*, 187 F.3d 24, 28-29 (1st Cir.),

cert. denied, 528 U.S. 1061 (1999); *Saenz v. Univ. Interscholastic League*, 487 F.2d 1026, 1027-1028 (5th Cir. 1973). Moreover, the MSA regime was endorsed by the other branches of government: The Superior Court of California expressly approved it, and the California Legislature passed the related statutes.[5]

4. Finally, petitioner is wrong in attributing to the Court of Appeals the holding that "the mere act of requesting [a law] . . . entitle[s] . . . the requesting party to have [its] conduct thereunder[] immunized." Pet. 34. Rather, the court recognized that the "conduct thereunder"—i.e., the post-MSA behavior—would *not* be immunized if that conduct would violate antitrust laws. *See* App. A20-21.

The Court of Appeals underscored the point when it correctly distinguished this case from *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976). App. A18-19. In *Cantor*, the private party's post-petitioning conduct was alleged to have been an antitrust violation in its own right. *Cantor*, 428 U.S. at 581-82. That is why the post-petitioning conduct did not enjoy *Noerr-Pennington* immunity. *See id.* at 601-02; *accord Greenwood Utils. Comm'n v. Miss. Power Co.*, 751 F.2d 1484, 1504 (5th Cir. 1985) (distinguishing *Cantor* on same ground). For petitioner to fit his case into the *Cantor* mold, he would have to have alleged that, subsequent to the MSA, the Manufacturers entered into an independ-

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[5] In any event, petitioner has never made this argument before; indeed, he conceded below that the challenged conduct constitutes "sovereign acts of the state." App. B11.

ent agreement to fix prices or restrict output. He does not, and could not, make any such allegation.

CONCLUSION

The petition for a writ of certiorari should be denied.

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In The
Supreme Court of the United States

STEVE SANDERS, Individually
and as Class Representative,

Petitioner,

v.

EDMUND G. BROWN JR., in his official capacity as Attorney General of the State of California; PHILIP MORRIS USA, INC.; R.J. REYNOLDS TOBACCO COMPANY; BROWN & WILLIAMSON TOBACCO CORPORATION; and LORILLARD TOBACCO COMPANY,

Respondents.

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QUESTIONS PRESENTED

1. Whether California state laws requiring tobacco manufacturers which do not settle certain liabilities through the Master Settlement Agreement ("MSA") to fund a reserve account for such liabilities are preempted on their face by the Sherman Act.

2. Whether tobacco manufacturers which settled certain liabilities through the MSA enjoy *Noerr-Pennington* immunity from Sherman Act liability for negotiating and complying with the MSA.

3. Whether California's acts of agreeing to the MSA and enacting related state laws are sovereign state acts that enjoy immunity from Sherman Act liability pursuant to the *Parker v. Brown* state action doctrine.

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Eugene Gressman et al., *Supreme Court Practice* Ch. 6.37(i)(3) (9th ed. 2007) 25

MMWR Weekly, 55(26), July 7, 2006; http://www.cdc/mmwr/preview/mmwrhtml/mm5526a2.htm 1

STATEMENT OF THE CASE

1. In November 1998, the attorneys general of California and most other states entered into the Master Settlement Agreement ("MSA"), the states' settlement of their litigation against the tobacco industry.[1] The states had sued the leading domestic tobacco manufacturers on the ground that they had illegally conspired to conceal the health risks of smoking and the addictiveness of nicotine, and for other alleged wrongs, including illegally marketing to minors. Through the MSA, the signatory states resolved their claims in exchange for commitments from the settling manufacturers to take steps to reduce the incidence of smoking, particularly among minors, and to assume significant financial responsibility for the public cost of past, present and future smoking.

The MSA's "public health" provisions include bans on advertising targeted at youth, the use of cartoons in advertising, and most outdoor advertising, as well as restrictions on brand name sponsorships and free sampling.[2] MSA § III(a)-(d) & (g). The

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[1] The four nonsignatory states – Florida, Minnesota, Mississippi, and Texas – already had settled their claims against the tobacco industry.

[2] The nationwide drop in youth smoking from 36.4% in 1997 to 23% in 2005 is an encouraging sign that the MSA's public health provisions are having a positive effect. *MMWR Weekly*, 55(26), July 7, 2006; http://www.cdc/mmwr/preview/mmwrhtml/mm5526a2.htm.

financial provisions require various payments, including annual payments which continue in perpetuity. MSA §§ VI(b), VIII(b) & (c), IX(b), (c) & (e) & XVII. The annual payments total $4.5 billion in 2000 and rise incrementally until they reach $9 billion in 2018. The signatory states are called the "Settling States" and the four manufacturers which negotiated the MSA are called the "Original Participating Manufacturers" or "OPMs."

Under the MSA, each OPM's share of the annual payment is determined by its "Relative Market Share" – i.e., its share of the OPM market in the year preceding the one in which the payment is due. MSA §§ II(mm) & IX(c)(1). This formula assures that each OPM pays the same amount per cigarette as every other OPM, and that each OPM's payment is commensurate with its sales volume and attendant harm to public health.

The MSA permits other tobacco manufacturers to sign the agreement and thereby settle their potential liabilities. MSA § II(tt). These companies are called "Subsequent Participating Manufacturers" or "SPMs." SPMs must comply with all of the MSA's public health provisions and with some of its financial provisions. MSA § IX(i)(1). Their annual payments correspond in amount to the OPMs' payments. To encourage prompt agreement, SPMs which sign the MSA within 90 days are obligated to make settlement payments only with respect to sales that exceed their 1998 market share or 125% of their 1997 market share, whichever is higher. MSA § IX(i).

Settling manufacturers are called "Participating Manufacturers" or "PMs." Non-settling manufacturers are called "Non-Participating Manufacturers" or "NPMs." NPMs are not subject to any obligations under the MSA and do not enjoy its liability release.

The MSA's annual payment is subject to various potential adjustments, including the NPM Adjustment. MSA § IX(c)(1). This adjustment, which is designed to protect the public health gains achieved by the MSA, reduces the annual payment under certain conditions. MSA § IX(d)(1). The adjustment, however, does not apply to any Settling State that enacts and diligently enforces the Model Statute, Exhibit T to the MSA, or some other "Qualifying Statute." MSA § IX(d)(1) & (2); Exh. T. California, like all other Settling States, has enacted the Model Statute as its Qualifying Statute. Cal. Health & Safety Code §§ 104555-104557.

California's Qualifying Statute establishes the policy that the public cost of smoking should be borne by tobacco manufacturers rather than the state to the extent that they either settle their liabilities with the state or are found culpable by the courts. *Id.* § 104555(d). The statute implements this policy by requiring every tobacco manufacturer to either: (a) become a Participating Manufacturer and generally perform its financial obligations under the MSA, or (b) deposit certain funds into an escrow account. *Id.* § 104557(a). The amount which must be deposited is based on the manufacturer's sales in California and is guaranteed not to exceed what the manufacturer

would have to pay as a PM. *Id.* § 104557(b)(2). Deposits not used to pay a tobacco-related liability to the state are released to the manufacturer after 25 years. *Id.* § 104557(b). This statute thus provides California with security for potential liabilities of non-settling tobacco manufacturers, and significantly reduces their MSA-related cost advantage.

In 2003 California strengthened its Qualifying Statute when it enacted additional legislation, sometimes called its "Contraband Amendment." This law requires each tobacco manufacturer to annually certify that it is in compliance with the Qualifying Statute and bans the sale of cigarettes produced by non-compliant manufacturers. Cal. Rev. & Tax Code § 30165.1(b), (c) & (e)(2).

2. According to the complaint, Petitioner Steve Sanders is a smoker and a California resident. Petitioner alleges that the OPMs are using the MSA, the Qualifying Statute and the Contraband Amendment to maintain an anti-competitive cartel and to charge supra-competitive prices. He alleges that the MSA is an "anticompetitive hybrid agreement" that allows PMs to raise prices without fear of losing sales or market share. He does not allege, however, that the MSA is an agreement to fix prices or restrict output. He also alleges that during the four years immediately after the MSA was signed, the OPMs raised prices by $12.20 a carton and their market shares did not "appreciably change."

Petitioner further alleges that California's Qualifying Statute and Contraband Statute should be declared invalid, and their enforcement enjoined, because they are preempted on their face by the Sherman Act. He alleges that his antitrust injury, which consists of illegally inflated cigarette prices, is "directly traceable" to these laws. Finally, Petitioner seeks damages from the tobacco manufacturer defendants under state antitrust law.

3. Both the California Attorney General and the tobacco manufacturer defendants timely moved to dismiss the action for failure to state a claim upon which relief could be granted. The district court granted the Attorney General's motion in the first instance on the ground that California's conduct was state action, insulated from Sherman Act liability under *Parker v. Brown*, 317 U.S. 341 (1943). App. B9-14. It found that the MSA is a sovereign act of the state of California and its MSA-related legislation is direct legislative activity. App. B11. It also ruled that *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980), does not apply because "the *Midcal* analysis is neither appropriate nor required for direct acts of the sovereign." App. B12.

The district court dismissed Petitioner's preemption claim because the MSA-related statutes do not irreconcilably conflict with federal antitrust law. App. B14-16. These statutes "do not mandate, permit or place irresistible pressure on manufacturers to take concerted action." App. B15. They mandate instead

"unilateral action by each to make settlement or escrow payments." *Id.* It also ruled that the California Attorney General enjoys *Noerr-Pennington* immunity from liability arising from its entry into the MSA. *Id.* at B16-18.

The district court dismissed the claims against the tobacco defendants on the grounds that they enjoy *Noerr-Pennington* immunity for their efforts to negotiate the MSA and that they enjoy both *Noerr-Pennington* and *Parker* state action immunity for their compliance with the MSA. App. B18-22. The district court also rejected Petitioner's contention that the MSA and related statutes are hybrid restraints. *Id.* at B21-22. A hybrid restraint, it ruled, is where government delegates regulatory power to private parties to enforce their own market decisions. The MSA is not a hybrid restraint because it "does not authorize collusive action among the manufacturers or give them the regulatory authority to set prices in the cigarette market." *Id.* at B21. It merely requires tobacco manufacturers to make certain unilateral settlement payments. *Id.* at B21-22.

4. The Court of Appeals for the Ninth Circuit affirmed. In a unanimous opinion authored by Judge Clifton, the court ruled that: (a) California's MSA-related statutes are not preempted by federal antitrust law, App. A12-14; (b) the tobacco defendants enjoy *Noerr-Pennington* immunity for their efforts to negotiate the MSA and for their compliance therewith, *id.* at A15-21; and (c) California enjoys *Parker* state action immunity for its negotiation of

the MSA and enactment of related legislation, *id.*, at A21-30.

The court of appeals rejected the preemption claim because it found that the challenged statutes were not in irreconcilable conflict with federal antitrust law. App. A12. Such a conflict can exist only if the state statute "'mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party' to violate those laws." *Id.* (quoting *Rice v. Norman Williams Co.*, 458 U.S. 654, 659 (1982).) The challenged statutes, the court found, do not explicitly allow any price-fixing, market division or other per se unlawful behavior, nor do they irresistibly pressure tobacco companies to fix prices. App. A12-13. Although they do force profit-seeking NPMs to factor their escrow costs into their prices, they do not force them "to either peg their prices to those of participating manufacturers, or to refrain altogether from entering the market." *Id.* at A13. If the leading PMs really are charging artificially high prices, the court noted, an NPM could compete on price with escrow costs factored in and earn a "normal" profit. *Id.*

The court also held that the tobacco defendants enjoy immunity under the *Noerr-Pennington* doctrine for their conduct in negotiating and complying with the MSA. App. A15-21. It ruled, first, that their negotiation of the MSA is immunized because it is a form of speech directed at a governmental entity. *Id.* at A17-18. It next determined that under *Allied Tube*

& Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988), and its own circuit precedent, *Noerr-Pennington* immunity also shields private parties from antitrust liability for injuries that result directly from the petitioned-for governmental action. *Id.* at A19-20. Because the injuries Petitioner alleged flowed directly from government action, his claims against the tobacco defendants failed. *Id.* at A21.

Lastly, the court held that California enjoys *Parker* state action immunity for agreeing to the MSA and enacting the related legislation. App. A21. After quoting *Parker* for the proposition that Congress did not intend to subject action directed by a state legislature to the Sherman Act, as well as its own precedents that *Parker* immunity extends to acts by judicial and executive branch officials, the court determined that "[t]he MSA thus fits the basic definition of 'state action' for *Parker* purposes." *Id.* at A23. The court next considered whether the MSA and related statutes are automatically immune under *Hoover v. Ronwin*, 466 U.S. 558 (1984), as sovereign state acts, or subject to *Midcal*'s two-part "clearly articulated"/"actively supervised" test. It held that *Hoover* "controls in cases where the state, acting as sovereign, imposes restraints on competition" and *Midcal* applies in situations where private parties participate in a state-authorized price-fixing regime. App. A28. Because the California Attorney General's decision to sign the MSA and the California Legislature's decision to pass the implementing legislation are sovereign acts which do not authorize private

parties to violate federal antitrust law, the court concluded that *Parker* immunity applies to these actions. *Id.*

REASONS FOR DENYING THE PETITION

Petitioner argues that certiorari is warranted to resolve what he calls "the intractable division among the courts of appeals on the validity of the MSA and its implementing legislation." Pet. 21. There is, however, no such "intractable division," and no need for intervention by this Court.

Contrary to Petitioner's assertion, the Second Circuit has not held that "the [MSA's implementing] statutes are preempted." *Id.* It merely held, in the context of reviewing an order granting a motion to dismiss, that these statutes "*would*" be preempted "were the allegations of the complaint proven." *Freedom Holdings v. Spitzer*, 357 F.3d 205, 232 (2nd Cir. 2004) (emphasis added). Moreover, on remand, the district court in *Freedom Holdings* strongly indicated that the allegations are false and that the challenged statutes are valid. *Freedom Holdings v. Spitzer*, 447 F. Supp. 2d 230, 259 (S.D. N.Y. 2004), *aff'd*, 408 F.3d 112 (2nd Cir. 2005). In short, a conflict among the circuits is unlikely to emerge.

Similarly, there is no conflict among the circuits regarding the scope of *Noerr-Pennington* immunity. The Ninth and the Third Circuits agree that *Noerr-Pennington* immunity protects private parties from

federal antitrust liability for complying with governmental mandates in the MSA and related state laws. And the Ninth Circuit's application of the *Noerr-Pennington* doctrine to the private conduct alleged here is perfectly consistent with Second Circuit's truism that the *Noerr-Pennington* doctrine is irrelevant to preemption claims against state statutes.

Petitioner's final ground for review, which asserts that the circuits are divided over *Midcal*'s place in antitrust law and its applicability to the MSA and related legislation, is another attempt to fabricate a non-existent conflict. The four circuits that have considered *Midcal* in the MSA context all agree that *Midcal* is used to determine whether restraints imposed by private parties with state sanction or enforcement are immune under the *Parker* state action doctrine; *Midcal* does not apply to restraints directly imposed by states acting in their sovereign capacities. Although they reach different conclusions as to whether or not the alleged MSA-related restraints may be subject to *Midcal*, their disparate results follow from their disparate treatment of the plaintiffs' conclusory allegations at the pleadings stage, not from disparate understandings of *Midcal*'s scope.

More generally, once the pending challenges to the MSA and related statutes reach final judgment in the various circuits, they may well all result in victories for the States. If one of these final judgments is adverse to the States, this Court would be free to settle any resulting conflict at that point. But this

Court would thwart, rather than promote, judicial economy if it granted certiorari now, before a genuine conflict has arisen and before some lower courts have adjudicated these claims.

In short, there is no genuine split amongst the circuits regarding the validity of the MSA and related state laws under federal antitrust law, and no fundamental difference of opinion over federal antitrust doctrine generally. The petition should be denied.

I. THE ASSERTED CIRCUIT CONFLICTS DO NOT EXIST

A. The Tension Among the Circuits Regarding Federal Antitrust Preemption of the MSA and Related State Laws Is Inchoate and Likely to Be Resolved by the Lower Courts

Petitioner's argument, Pet. 20-23, that the federal appeals courts are intractably divided on whether or not the Sherman Act preempts MSA-related state laws is simply wrong. First, all three appellate courts that have considered the matter agree that such preemption claims are subject to the "irreconcilable conflict" test set forth in *Rice*, 458 U.S. at 659. *Sanders*, App. A12; *Tritent v. Commonwealth of Kentucky*, 467 F.3d 547, 554 (6th Cir. 2006); *Freedom Holdings v. Spitzer*, 357 F.3d 205, 222 (2nd Cir. 2004).

Second, contrary to Petitioner's assertion, Pet. 21-22, the Second Circuit did not hold that New York's MSA-related laws were preempted. Rather, it held that the *Freedom Holdings* complaint, which alleged that these laws enforced an express market-sharing agreement among private parties, stated a valid claim for preemption. *Freedom Holdings*, 357 F.3d at 224, 226, 235. In other words, the Second Circuit merely decided that a preemption claim had been adequately pled. Whether or not the challenged laws actually operated in the manner alleged, and therefore were preempted, was a matter that the Second Circuit remanded to the district court for decision.

Hence, the "conflict" among the circuits is nothing more than possible tension between the Second Circuit's holding that the complaint it reviewed adequately alleged a preemption claim, and the Sixth and Ninth Circuits' holdings that the complaints they reviewed did not. Moreover, this tension appears entirely attributable to the courts' slightly differing views of their obligation to accept the allegations of the complaint as true. Unlike the Sixth and Ninth Circuits, which independently examined the challenged statutes and the MSA, *Trident*, 467 F.3d at 554-55, *Sanders*, App. A11-13, the Second Circuit uncritically accepted plaintiffs' allegations, a point which it repeatedly made in its ruling, *Freedom Holdings*, 357 F.3d at 208, 209, 216, 225, & 230.

Furthermore, subsequent rulings favoring New York strongly suggest that the final result in the

Second Circuit will accord with those already reached in other circuits. Since the Second Circuit's ruling in *Freedom Holdings*, both the district court in that case and another district court in New York have preliminarily rejected preemption challenges to MSA-related laws.

In the *Freedom Holdings* case after remand, the district court refused to preliminarily enjoin enforcement of the MSA and related laws because "plaintiffs have not shown a likelihood that the MSA and the Escrow and Contraband Statutes constitute a per se violation of the Sherman Act." *Freedom Holdings*, 447 F. Supp. 2d at 254. It found that "[t]he facts as proved . . . tell a quite different story" from the one alleged in the complaint, *id.* at 248, and that the "evidence seems to fit more closely with the State's view," *id.* at 258. Among other things, the court found that the escrow costs of the non-settling companies are lower than the MSA costs of most settling companies, and operate essentially as a flat tax. *Id.* at 238-40, 258. It also found that during the five years immediately following the MSA, the non-settling companies gained considerable market share (their market share rose from .5% to 8.2%), and the leading settling companies lost substantial market share (their market share dropped from 96.5% to 84.5%). These and other hard facts about the MSA, the related legislation, and the post-MSA cigarette market proved that plaintiffs' fundamental allegation that the MSA scheme is anticompetitive was untrue. The evidentiary record established instead that the MSA and the related

statutes have had "no adverse competitive impact on the [non-settling] NPMs." *Id.* at 241.

In *Grand River Enterprises v. Pryor*, No. 02 Civ. 5068 (JFK), 2006 U.S. LEXIS 35614 (2006), *aff'd on other grounds*, 481 F.3d 60 (2nd Cir. 2007), another district court in New York refused to enjoin enforcement of escrow statutes enacted by thirty-one states based upon its independent finding that such laws would likely survive federal antitrust preemption challenge. The court found that the statutes probably are not preempted because they require each cigarette manufacturer to "make its own unilateral decision with respect to price and output, and no state agent has the power to dictate the prices or output of any cigarette manufacturer." *Id.* at *25.

These rulings thus foreshadow final outcomes in the Second Circuit fully consistent with those reached by the Sixth Circuit and in the court below, and provide ample reason to deny review. There simply is no need to resolve now a potential conflict that is unlikely to mature into a serious division among the circuits. In the improbable event that such a conflict does arise, review may be sought at that time.

Denying review now also is potentially advantageous because it may give the Court the benefit of the views of two other appeals courts on the same subject. The Tenth Circuit presently has under submission two appeals which involve federal antitrust preemption challenges to Qualifying Statutes. *Xcaliber v. Morrison*, No. 06-3071 (10th Cir. argued Sept. 25,

2006); *Xcaliber v. Edmondson*, No. 05-5178 (10th Cir. argued Sept. 25, 2006).[3] In addition, an appeal of another judgment upholding a Qualifying Statute against federal antitrust preemption challenge was recently filed in the Eighth Circuit. *Grand River Enterprises v. Beebe*, 418 F. Supp. 2d 1082 (W.D. Ark. 2006), *appeal docketed*, No. 08-1436 (8th Cir. Feb. 26, 2008).

B. There Is No Conflict Among the Circuits or with the Decisions of the Court Regarding the Scope of *Noerr-Pennington* Immunity.

Petitioner asserts that review should be had to resolve "growing conflict and confusion" among the federal circuits over the scope of the *Noerr-Pennington* doctrine.[4] Pet. p. 22. According to Petitioner, there is a conflict between the Third and Ninth Circuits, on the one hand, and the Second

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[3] The *Edmondson* appeal seeks review of an order granting Oklahoma's summary judgment motion on the grounds that its Allocable Share Amendment to its Qualifying Statute was not preempted and not a hybrid restraint. *Xcaliber v. Edmondson*, No. 04-CV-0922-CVE-PJC, 2005 U.S. Dist. LEXIS 26705 (N.D. Okla. 2005). The *Morrison* appeal seeks review of a parallel order issued by the district court in Kansas. *Xcaliber v. Kline*, No. 05-2261-JWL, 2006 U.S. Dist. LEXIS 77420 (Kan. 2006).

[4] The *Noerr-Pennington* doctrine traces back to *United Mine Workers of America v. Pennington*, 381 U.S. 657 (1965), and *E.R.R. Presidents Conf. v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961).

Circuit and this Court, on the other, over whether or not *Noerr-Pennington* immunity protects private parties from Sherman Act liability for complying with petitioned-for governmental mandates in the MSA and related state laws. Pet. 23.

Such a conflict, however, does not ex . The two circuits that have reached this issue – i.e., the Third and the Ninth – agree that *Noerr-Pennington* immunity applies to such conduct. *Sanders*, App. A20-21; *A.D. Bedell Wholesale Co. v. Philip Morris, Inc.*, 263 F.3d 239, 251 (3rd Cir. 2001), *cert. denied*, 534 U.S. 1081 (2002). The Second Circuit is not in conflict with its sister circuits on this question. The Second Circuit did not rule on this issue in *Freedom Holdings* because it was not presented for decision, there being no private defendants in the case to assert the matter.

The issue which the Second Circuit did address – whether *Noerr-Pennington* immunity protects "anti-competitive legislation from being held to be pre-empted as in conflict with the *Sherman Act*," *Freedom Holdings*, 357 F.3d at 233, – is one on which the circuits apparently are in accord. Although the Ninth Circuit declined to decide the issue in this case because it was not raised, it carefully noted that the Second Circuit "may be correct" on this point. Pet. App. A21, n.9.

Nor is there any conflict between the Third and Ninth Circuit rulings and Supreme Court precedent. To the contrary, the rulings of both courts are faithful to *Allied Tube & Conduit Corp. v. Indian Head, Inc.*,

486 U.S. 492, 499 (1988), wherein the Court held that "where a restraint upon trade . . . is the result of valid governmental action . . . , those urging the governmental action enjoy absolute immunity from antitrust liability for the anticompetitive restraint. . . ." They also accord with *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976), on which Petitioner relies. In *Cantor*, a plurality decided that *Noerr-Pennington* immunity does not extend to independent antitrust violations occurring after successful government petitioning. Because Petitioner's complaint is based upon injuries "caused directly by governmental action," App. A21, and not on any independent antitrust violation, the opinion below does not conflict with *Cantor*.

C. There Is No Circuit Split over *Midcal's* Place in Federal Antitrust Law and the Supposedly Different Analyses Regarding *Midcal's* Applicability to the MSA and Related State Laws are Easily Reconciled.

According to Petitioner, the decision below expands a preexisting circuit split over whether or not a state scheme that fails the *Midcal* test nevertheless can receive *Parker* state action immunity. Pet. 25. The supposed circuit split, with the Second and Third Circuits on one side, and the Sixth and Ninth Circuits on the other, however, does not exist. All four appeals courts agree that a state statutory scheme that is subject to, and fails, the *Midcal* test does not qualify as antitrust-exempt state action. *Sanders*,

App. A24; *Tritent*, 467 F.3d at 554-55 (a statute that mandates or authorizes per se illegal conduct in all instances will be saved from preemption by the *Parker* state action doctrine only if it satisfies *Midcal*); *Freedom Holdings*, 357 F.3d at 223 (state statute that permits or compels private parties to engage in per se violations will be saved from preemption only if it satisfies *Midcal*); *Bedell*, 263 F.3d at 254 (state-authorized, but privately-imposed restraints qualify as state action only if they satisfy *Midcal*).

All four circuits also agree on *Midcal*'s place in federal antitrust law. The *Midcal* test applies to determine whether a statute (unlike these) that is preempted under *Rice*, is nevertheless "saved" from preemption, and whether private conduct pursuant to such a statute qualifies as immunized state action. The *Midcal* test does not apply to restraints directly imposed by the state acting as sovereign. *Sanders*, App. A23, A26-28 (*Midcal* test needed to decide whether private conduct pursuant to a state statute gets *Parker* immunity); *Tritent*, 467 F.3d at 554-58 (*Midcal* applies to a state law which authorizes or mandates per se unlawful private conduct); *Freedom Holdings*, 357 F.3d at 222-23 (same); *Bedell*, 263 F.3d at 255 ("When it is uncertain whether an act should be treated as state action for the purposes of Parker immunity, we apply the test set forth in . . . *Midcal*").

The circuits diverge only with respect to the specific question of whether the complaints adequately allege claims that make *Midcal* applicable to the MSA and related legislation, and their divergent

answers are readily reconciled. The Second Circuit's ruling that *Midcal* did apply followed from its prior determination that the complaint had adequately alleged a claim for facial preemption under *Rice*. *Freedom Holdings*, 357 F.3d at 226. The Sixth Circuit's contrary ruling in *Tritent*, 467 F.3d at 558, flowed from its antecedent determination that the complaint did not adequately allege such a claim. Had the Second Circuit concluded that a claim of facial preemption had not been adequately alleged, it undoubtedly would have ruled, like the Sixth Circuit, that *Midcal* did not apply. And had the Sixth Circuit found the complaint adequate, it would have, like the Second Circuit, subjected the statutes to *Midcal*. These rulings thus follow from differences in the underlying pleadings, or judicial interpretations thereof, rather than from any disagreement over *Midcal* itself.

The same is true for any asserted inconsistency between the ruling in *Bedell* and the decision below. In *Bedell*, the Third Circuit stated that *Midcal* applied to the alleged conduct because the plaintiffs traced their alleged injuries mainly to conduct by the private tobacco companies, not to government action.[5]

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[5] Because the *Bedell* court affirmed the dismissal of the action on *Noerr-Pennington* grounds, its discussion of *Parker* immunity was unnecessary to its disposition of the case. However, in *Mariana v. Fisher*, 338 F.3d 189 (3rd Cir. 2003), *cert. denied*, 540 U.S. 1179 (2004), a subsequent challenge to the MSA and related legislation brought against state officials, the Third Circuit revisited the *Parker* immunity issue. After affirming the dismissal of the action on *Noerr-Pennington* grounds, the court

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Bedell, 263 F.3d at 258. In the decision below, the Ninth Circuit ruled that *Midcal* did not apply because Petitioner traced his asserted injury to government, not private, action. Pet. App. A28. Both circuits agree with the rule of law that direct action by the state acting as sovereign is not subject to *Midcal*. *Bedell*, 263 F.3d at 255 ("[a]pplying Midcal is unnecessary if the alleged antitrust injury was the direct result of a clear sovereign state act"); *Sanders*, App. A28 ("*Hoover* therefore controls in cases where the state, acting as a sovereign, imposes restraints on competition. The state in such situations is immune from antitrust liability, regardless of whether the restraint in question would satisfy the *Midcal* test."). Thus, any tension between the Ninth and Third Circuits, like that between the Second and Sixth, is due to differing treatment of conclusory factual allegations, not to divergent understandings of federal law on antitrust preemption. Such minor discrepancies do not warrant the Court's attention.

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rejected the state officials' *Parker* immunity defense because it believed it was bound by *Bedell* and that *Bedell* assumed that state officials do not enjoy *Parker* immunity. *Id.* at 203-04. In so doing, however, it acknowledged that *Bedell's* analysis of *Parker* immunity was questionable, *id.* at 203, and that "[c]ritics may with some justification regard our discussion of *Parker* immunity as dictum," *id.* at 204.

II. THE OTHER ASSERTED GROUNDS FOR REVIEW LACK MERIT

A. The Decision Below Does Not Implicate Recurring Questions of National Importance.

1. Petitioner also requests review on the grounds that the validity of the MSA, its implementing legislation and tobacco company conduct thereunder are questions of great practical importance and recurrent litigation, and that "continuing uncertainty" about their validity is assertedly "harmful to all involved." Pet. 27-28. The MSA and related legislation are undeniably important. As this Court noted, the MSA is a "landmark" agreement, *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525, 533 (2001), which promotes public health in numerous important ways and provides Settling States with much-needed compensation for the enormous harm caused by cigarette smoking.[6] The implementing legislation likewise provides Settling States with security for non-released tobacco liabilities and protects against MSA-related unfair competition from non-settling tobacco companies.

There is, however, no serious question about the validity of the MSA and related state laws. To the contrary, the lower courts have, with remarkable

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[6] Tobacco use is perhaps "the single most significant threat to public health in the United States." *FDA v. Brown & Williamson*, 529 U.S. 101, 161 (2000).

consistency, rejected federal antitrust challenges to the MSA and implementing state laws. Every single district court that has entered a final judgment on such a claim has ruled in the State's favor, and every single federal appeals court has affirmed. *Sanders*, App. A31 (dismissal of Sherman Act claim affirmed); *Tritent*, 467 F.3d at 559 (same); *Mariana*, 338 F.3d at 200 (same); *Bedell*, 263 F.3d at 252 (same); *Int'l Tobacco Partners v. Kline*, No. 05-2319-KHV, 2007 U.S. Dist. LEXIS 9359, *20-28 (D. Kan. 2007) (Sherman Act claim denied on summary judgment); *Int'l Tobacco Partners v. Beebe*, 420 F. Supp. 2d 989, 994-97 (W.D. Ark. 2006) (Sherman Act claim dismissed for failure to state a claim); *Grand River Enterprises*, 418 F. Supp. 2d at 1089-91 (same); *Dos Santos v. Beebe*, 418 F. Supp. 2d 1064, 1071-73 (W.D. Ark. 2006) (same); *Xcaliber v. Kline*, No. 05-2261-JWL, 2006 U.S. Dist. LEXIS 77420 (Kan. 2006) (Sherman Act claim denied on summary judgment), *appeal docketed*, No. 06-3061 (10th Cir.); *S & M Brands, Inc. v. Summers*, 393 F. Supp. 2d 604, 629-30 (M.D. Tenn. 2005) (same), *aff'd*, 228 Fed. Appx. 560, 562-63 (6th Cir. 2007); *Xcaliber v. Edmondson*, No. 04-CV-0922-CVE-PJC, 2005 U.S. Dist. LEXIS 26705 (N.D. Okla. 2005) (Sherman Act claim rejected on summary judgment), *appeal docketed*, No. 05-5178 (10th Cir.); *North Am. Trading Co. v. Nat'l Ass'n Attys Gen.*, Civ. No. 01-01600, (D. D.C. Sept. 18, 2001), *aff'd*, No. 01-7173 (D.C. Cir. Nov. 25, 2002); *PTI v. Philip Morris*, 100 F. Supp. 2d 1179, 1191-97 (C.D. Cal. 2000) (Sherman Act claim dismissed for failure to state a claim); *Hise v. Philip Morris*, 46 F. Supp. 2d 1201, 1209 (C.D. Cal.

2000) (Sherman Act claim rejected on summary judgment), *aff'd*, 208 F.3d 226 (10th Cir. 2000) (unpublished decision), *cert. denied*, 531 U.S. 959 (2000).

Contrary to Petitioner's assertion, Pet. 28-29, the States did not acknowledge uncertainty about the validity of the MSA and related legislation in their petition for certiorari to review the Second Circuit's decision in *Grand River Enterprises v. Pryor*, 425 F.3d 158 (2005), *cert. denied*, 127 S. Ct. 379 (2006). That petition concerned the distinct jurisdictional question of whether judicial review of a state law should be had by a federal court located in the state where the law was enacted or whether, as the Second Circuit erroneously held, such review may be had by a federal court located in some other state, depending upon the circumstances of the case. As the States' *Grand River* petition correctly observed, the availability of multiple forums for such review threatens "the certainty and finality that ordinarily results from decisions rendered by federal courts (particularly federal courts of appeals) in their respective States." Pet. 28 (quoting 2006 WL 1049019, at *14-*15.) This expression of concern about the certainty and finality of federal court decisions, however, is by no means an acknowledgment that there is doubt about the validity of the MSA and related legislation.

In short, there is very little doubt about the validity of the MSA and related state laws. Such residual doubt does not impair government budgeting or corporate planning, nor does it warrant Supreme Court review.

2. Petitioner seeks review on the additional ground that the questions presented are of general importance to the "proper implementation of antitrust law generally." Pet. 29-30. Petitioner argues that the court below reached a result that "essentially renders . . . [*Midcal*] a dead letter in most circumstance[s]." *Id.* at 30. This assertion, however, cannot be squared with the Ninth Circuit's decision, which recognizes *Midcal*'s proper place in antitrust jurisprudence and correctly rules that the restraints Petitioner challenged are direct state acts not subject to *Midcal*.

In this case, the Ninth Circuit held that *Midcal* applies to state statutes that authorize or require private parties to engage in per se violations of federal antitrust law and to hybrid restraints such as the scheme at issue in *Midcal;* it does not, however, apply to restraints directly imposed by the state. App. A28. This understanding of *Midcal*'s reach is consonant with *Parker*'s key holding that when Congress passed the Sherman Act it did not intend to limit the states' freedom to regulate markets, and with the Court's subsequent decisions, which apply *Midcal* to private antitrust violations pursuant to state directive, but not to direct state action. *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 632-40 (1992) (*Midcal* applied to determine whether rate-setting by private title insurers was protected by *Parker* immunity); *S. Motor Carriers Rate Conf. v. United States*, 471 U.S. 48, 61 (1985) (*Midcal* "appli[es] to private parties' claims of state action immunity"); *Hoover*, 466 U.S. at 568-69 ("[w]here the conduct at issue is in fact that of the

state legislature or supreme court, we need not address the issues of 'clear articulation' and 'active supervision'").

The decision below also conforms to the logic behind the *Midcal* test. This test, which asks whether the restraint is "clearly articulated and affirmatively expressed as state policy" and "actively supervised by the state," is a useful tool for determining whether private action pursuant to state authorization or directive is truly state action. It is unnecessary and nonsensical, however, as applied to restraints directly imposed by the state, because such restraints are clearly matters of state policy for which supervision is unnecessary. Thus, far from treating *Midcal* as a virtual dead letter, the court below afforded *Midcal* its proper scope, and correctly concluded that because the restraints that Petitioner challenged were direct acts by the state of California, *Midcal* did not apply.[7]

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[7] Petitioner's final argument that the MSA scheme implicates the constitutional prohibition against unapproved interstate compacts, Pet. 31-32, merits little reply. His complaint does not allege a violation of the Interstate Compact Clause, and it is far too late in the day to allege one now, even obliquely through an assertion that this constitutional provision is somehow "implicate[d]." Eugene Gressman et al., *Supreme Court Practice*, Ch. 6.37(i)(3) (9th ed. 2007). Moreover, such claims have been consistently rejected by other courts. *Star Scientific, Inc. v. Beales*, 278 F.3d 339, 357-360 (4th Cir. 2002), *cert. denied*, 537 U.S. 818 (2002); *PTI*, 100 F. Supp. 2d at 1197-98; *Hise*, 46 F. Supp. 2d at 1210 (Interstate Compact clause claim rejected as "plainly frivolous"); see generally, *Mariana*, 338 F.3d 189 at 204-06 (Interstate Compact Clause claim rejected for lack of standing).

B. The Decision Below Correctly Applied Settled Antitrust Immunity Principles to the MSA and Related State Laws.

Contrary to Petitioner's assertion, Pet. 32-35, the decision below is correct and affords no reason for review. It applied the correct "irreconcilable conflict" test to his claim of facial preemption. App. A12-14. Petitioner's assertion now that his preemption claim was actually an "as-applied" challenge, and subject to a different legal standard, is untrue. His complaint does not contain an "as-applied" claim and only seeks a judgment declaring that California's Qualifying Act and Contraband Amendment are "facially void as a *per se* restraint of trade." App. A10, n.6.

The conclusion by the court below that the MSA and related statutes are sovereign state acts, not hybrid restraints, is likewise correct. Both the MSA and California's related state laws impose unilateral obligations on tobacco manufacturers to make certain payments either directly to the Settling States or into an escrow account. They do not require or permit them to fix prices, divide markets, restrict output, or engage in any other conduct forbidden by federal antitrust law.

Nor is the MSA scheme a hybrid restraint. A hybrid restraint is where government delegates to private parties power to regulate trade. *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345, n.8 (1987); *Fisher v. City of Berkeley*, 475 U.S. 260, 267-68 (1986). A state

law which allows private parties to dictate other companies' prices, for example, is a hybrid restraint.

The MSA and the related state laws do no such thing. California does not enforce any tobacco manufacturer's pricing decisions or permit any tobacco manufacturer to control the pricing of others. It merely enforces their obligations to make certain settlement payments or escrow deposits. Every court to consider the matter on a factual record has so ruled. *Int'l Tobacco Partners*, 2007 U.S. Dist. LEXIS 9359, *25-27; *Xcaliber*, 2006 U.S. Dist. LEXIS 77420, *14; *Grand River*, 2006 U.S. Dist. LEXIS 35614, *25; *Xcaliber*, 2005 U.S. Dist. LEXIS 26705, *18; but see *Bedell*, 263 F.3d at 259 (per allegations of complaint, MSA "resembles" hybrid restraint).

CONCLUSION

The petition for writ of certiorari does not satisfy the Court's standards for discretionary review and should be denied.

Dated: April 1, 2008

Respectfully submitted,

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No. 07-995

In The

Supreme Court of the United States

STEVE SANDERS,
individually and as class representative
Petitioner,

v.

EDMUND G. BROWN, in his official capacity as Attorney General of the State of California, PHILIP MORRIS USA, INC., R.J. REYNOLDS TOBACCO CO., BROWN & WILLIAMSON TOBACCO CORP., and LORILLARD TOBACCO CO.,
Respondents.

On Petition for Writ of Certiorari
To the United States Court of Appeals for the Ninth Circuit

REPLY IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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STATEMENT OF THE CASE

Respondents do not deny that under the MSA the Original Participating Manufacturers ("OPMs") have increased prices well beyond that necessary to fund their MSA payment obligations. Nor do they deny that price increases have occurred in lockstep among the OPMs. The nevertheless offer the distinctly factual claim that the MSA merely imposes a uniform charge per cigarette sold on each OPM independent of market share or volume and that the OPMs are merely complying with independent obligations to pay such fees.

But the MSA's complex payment allocation scheme show those assertions to be incorrect or, at best, subject to ample factual dispute.[1] For example, the per-cigarette charge on the OPMs is not fixed or uniform except in the first instance. Increases in price by one OPM, if not met by the others, would both reduce the relative market share of that manufacturer, reduce the total volume of the aggregate OPM market share to some degree (and shift volume to the other OPMs in part as well), and thus *disproportionately* change the relative market share among the OPMs. That disproportionate change in market share would result

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[1] The MSA's complex and interdependent allocation scheme itself, spanning dozens of pages of the agreement, tends to belie the notion of a fixed charge per cigarette, which could have been provided for in a few sentences as with the escrow charges applied to NPMs. The Second Circuit recognized as much in describing the MSA payment scheme and distinguishing it from a fixed charge per cigarette. *See Freedom Holdings Inc.* v. *Spitzer*, 357 F.3d 205, 228-29 (CA2 2004) ("*Freedom Holdings I*").

in the lower-priced manufacturers paying a greater per-cigarette cost than would the higher-priced manufacturer.

In any event, the complex interaction of the MSA's dozens of pages of allocation rules is not an issue this Court needs to or can resolve at this stage of the litigation. It is sufficient that the complaint reasonably alleges an interdependency between the OPMs that affects and can change the per-cigarette charge and that encourages each OPM to match price rises by the others in order to maintain the balance of the MSA payments and not be subjected to higher relative payments. Far from imposing *independent* obligations on individual manufacturers, the MSA institutionalizes a *dependency among* the OPMs whereby the pricing decisions of one OPM drives parallel pricing decisions by the others.

REASONS FOR GRANTING THE WRIT

As Respondents acknowledge, the MSA is "perhaps the most far-reaching and important" settlement in history, affecting hundreds of billions of dollars and the national market in cigarettes. Mfrs. BIO at 1; AG BIO at 21. The sheer scope and effect of the settlement is precisely what makes the application of uniform legal rules regarding antitrust immunity a matter of national importance and worthy of this Court's attention.

I. There Is an Extended Split on the Questions Presented.

Denying the splits expressly acknowledged by the Ninth Circuit below, Respondents claim that there is no split because no court has entered final judgment

against them. Mfrs. BIO at 18-19, 22-23, 26; AG BIO at 12-14. But, as the Ninth Circuit itself recognized, the circuits have split – genuinely so – on certain essential legal questions governing the eventual resolution of much of the litigation involving the MSA. Pet. 16, 18-19; App. A13, A21, A24. That the rulings have occurred at the motion to dismiss stage rather than after trial does not demonstrate a mere "procedural" dispute – as the Manufacturers would have it – but in fact demonstrates that the differences are based on clean disputes as to the substance of antitrust law based on comparable allegations regarding the MSA and its consequences. *Cf.* Mfrs. BIO at 2 (current suit offers "no new allegations or legal theories" than other suits).

The wholly separate question whether such allegations will prove out at trial are not relevant at the motion to dismiss stage, and Respondents' bold assertions that the eventual facts will support the same *result* are particularly inappropriate given that Petitioner here and plaintiffs elsewhere generally have not been given the opportunity to prove their facts and put on expert economic testimony concerning the effects of complex allocation scheme under the MSA.

A. The Decision Below Expands the Split on Preemption.

The Second and Ninth Circuits, both evaluating the allegations of comparable complaints, as well as the MSA provisions referenced therein, have reached opposite conclusions regarding whether the MSA and its related statutes would be preempted based on such allegations. Pet. 16, 20-21. Contrary to Respondents' suggestions, Mfrs. BIO at 21, the Second Cir-

cuit did not blithely ignore the provisions of the MSA, but instead carefully examined those provisions as well as the allegations regarding their effect, and found them sufficient to state a *per se* antitrust violation. *Freedom Holdings I*, 357 F.3d at 226. While Respondents are, of course, correct that the Second Circuit's preemption holding was based on alleged facts that would eventually be tested at trial, that does not change the fact that the case squarely splits with the present Ninth Circuit decision, which similarly ruled on the allegations, not the eventual facts of a trial.[2] On comparable alleged facts, therefore, the two circuits reached opposite holdings as a matter of law – the quintessential description of a split.

Respondents try to pass off the difference in the circuit rulings as attributable to the Second Circuit's supposed inattention to the terms of the MSA and its acceptance of supposedly incorrect allegations. Mfrs. BIO at 20-21; AG BIO at 12-13. But the Second Circuit discussed the terms and operation of the MSA in detail and explained how they were reasonably alleged to have anticompetitive effects and how they differed from a fixed per-cigarette charge. *Freedom Holdings I*, 357 F.3d at 210-11, 225-26, 228-29. The

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[2] Petitioner, of course, does not claim that the Second Circuit rendered a final decision on the ultimate merits of the preemption claim, merely that it found the allegations sufficient to demonstrate preemption, as the quotes of the Second Circuit in the Petition indicated. Pet. 25-26. Petitioner does not mean to suggest otherwise any more than did the Ninth Circuit in describing the holdings of the Second and Third Circuits. *See* Mfrs. BIO at 23 n. 2; App. A28-A29. The split identified goes not to the ultimate outcomes of the cases, but rather to the conflicting *legal holdings* on virtually identical alleged facts.

Second Circuit thus gave precisely the type of attention to the allegations and the MSA that this Court described in its recent decision in *Bell Atlantic Corp.* v. *Twombly*, 127 S. Ct. 1955 (2007), and found the alleged anticompetitive injury sufficiently persuasive to defeat a motion to dismiss.

That later proceedings in the Southern District of New York and the Second Circuit denied a preliminary injunction hardly undermines the existence of a split on the underlying legal question. *Freedom Holdings, Inc.* v. *Spitzer*, 447 F. Supp.2d 230 (S.D.N.Y. 2004), *aff'd*, 408 F.3d 112 (CA2 2005). The problems of proof noted by the Southern District of New York were evaluated under a heightened standard applied to requests for preliminary injunctions that would change the status quo, 447 F. Supp.2d at 247, and, in relevant part, went largely to the issue of whether the MSA injured *NPMs* relative to OPMs, not whether it reduced competition among OPMs and injured *consumers*. 447 F. Supp.2d at 254-59. The Second Circuit's affirmance of that denial of a preliminary injunction was based upon the lack of irreparable harm to the NPMs, 408 F.3d at 114-15, not on that court's agreement with the district court regarding the effects of the MSA. And, of course, neither of those courts questioned the earlier legal rulings in *Freedom Holdings I*.[3]

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[3] Furthermore, the district court's determination that the escrow obligations on *NPMs* were essentially a flat tax that did not preclude price competition *above* the newly imposed price floor hardly negates the anti-competitiveness of creating such an artificially higher floor for NPMs in the first place. And, in any event, the district court recognized the difference between the

B. *The Decision Below Expands A Split on the Application of the* Noerr-Pennington *Doctrine.*

Regarding the *Noerr-Pennington* doctrine, the conflict identified in the Petition was on whether *Noerr-Pennington* immunized the "results" of petitioning activity rather than merely the petitioning itself. Pet. 23. Contrary to Respondents' suggestion, Mfrs. BIO at 24, whether the results being considered are the government action itself as in *Freedom Holdings I*, or the private conduct facilitated by such government action, as here, does not change the question or the correct answer. The results of petitioning – both the government action and the private conduct thereunder – must be evaluated under *Parker* (and *Midcal* in the case of a hybrid restraint), not under *Noerr-Pennington*. The Ninth Circuit, however, refused to apply *Parker* to the resulting conduct by the OPMs, misconceiving the legal scope of *Noerr-Pennington* immunity. That the Second Circuit correctly limited *Noerr-Pennington* and instead applied *Parker* and *Midcal* to the *governmental* results of petitioning, as opposed to the subsequent private conduct thereunder, still presents a split on the relevant legal question. The two situations both turn on the same issue of the scope of *Noerr-Pennington* and whether it extends beyond petitioning activity itself.[4]

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flat per-cigarette charge imposed on NPMs and the complex charges to OPMs resulting from the MSA's allocation scheme. 447 F. Supp.2d at 238.

[4] Contrary to Respondents' suggestion, Mfrs. BIO at 25, Petitioner certainly does allege that the OPMs' conduct *following* the MSA, not merely entry into the MSA itself, is illegal. *See* Pet. at 8-9, 17-18. And, and as the Second Circuit has recognized, there is no need to allege a further agreement among the

C. *The Decision Below Expands the Split Regarding the Application of the* Midcal *Test.*

The essential dispute among the circuits regarding *Midcal* turns on what constitutes a hybrid restraint that would be subject to the *Midcal* analysis. Pet. 25-26. Respondents' and the Ninth Circuit's denials that the MSA enables or facilitates private anticompetitive conduct, Mfrs. BIO at 22, App. A28, simply state one side of that split based on improperly restrictive criteria for finding hybrid restraints. The Second and Third Circuits, however, both viewed the MSA, as alleged, to be a hybrid restraint.[5] It is on the legal standards for finding a hybrid restraint that he courts diverge, not on any difference in the alleged facts.

OPMs where the MSA itself was an agreement among the OPMs, not merely with the state AGs, and the MSA established the market conditions that facilitated and drove interdependent and coordinated conduct. *Freedom Holdings I*, 357 F.3d at 223-24.

[5] The suggestion, Mfrs. BIO at 23-24, that the Third Circuit's *Parker/Midcal* holding is merely *dicta* is contrary to how the Third Circuit itself treats that holding, notwithstanding the misgivings of particular judges. *See Mariana* v. *Fisher*, 338 F.3d 189, 202, 203 (CA3 2003) ("Because this court in *Bedell* examined precisely the same facts and the same documents and concluded that we must apply the *Midcal* test, we believe we are not free to decide to the contrary."; "Nonetheless, even though the case before us differs from *Bedell* in that the parties are different, we feel bound by *Bedell* to abstain from reaching a different conclusion on *Parker* immunity. We cannot in conscience characterize the discussion on *Parker* immunity in *Bedell* as dicta."), *cert. denied*, 540 U.S. 1179 (2004).

II. The Circuit Split Implicates Recurring Questions of National Importance.

1. As the Petition explained, at 28-29, the disparate rules applied by the circuits have created uncertainty regarding the MSA and its state statutes, particularly where the Second Circuit has asserted jurisdiction over state AGs from around the country. Respondents' claimed confidence as to the eventual outcomes of any cases that might reach trial, Mfrs. BIO at 26; AG BIO at 21-22, seems more like puffery than a genuine lack of uncertainty. Indeed, while Respondent Attorney General now denies any uncertainty from the current conflict between the circuits, AG BIO at 23, the Petition of the State AGs in *Grand River* is quite to the contrary. Petition for Writ of Certiorari of State Attorneys General, No. 05-1343, 2006 WL 1049019, at *14-*15 (Apr. 18, 2008), seeking review of *Grand River Enterprises Six Nations, Ltd.* v. *Pryor*, 425 F.3d 158 (CA2 2005), *cert. denied*, 17 S. Ct. 379 (2006). That petition decried the loss of "certainty and finality" for decisions favorable to the States in other jurisdictions, thus necessarily recognizing that Second Circuit jurisdiction – coupled with the different legal standards applied in that circuit – threatens to undermine favorable rulings elsewhere. Uniform standards, for whatever legal rule this Court endorses, would at least provide legal certainty and consistency as to the test to be applied, whether favorable or unfavorable to the MSA.

Respondents suggest, Mfrs. BIO at 27, that other pending cases would make better vehicles if and when this Court decides to take up the issues here. But there is no need to await further percolation – or

to wait for cases involving summary judgment – where the legal issues and disagreements are directly addressed by the Ninth Circuit. Waiting only prolongs the time when challenges to the MSA receive the full factual development they deserve (or prolongs litigation in the Second Circuit if this Court eventually agrees with the Ninth Circuit).[6] Furthermore, cases arising from summary judgment raise the risk that they will turn on factual matters or case-specific failures of proof rather than on purely legal questions. Cases arising from motions to dismiss – based on complaints that are not meaningfully different – thus present cleaner vehicles through which this Court can address the legal issues in dispute.

2. Regarding the importance of this case to antitrust law in general, Respondents claim that the court below was faithful to *Midcal* and thus there is no confusion in the legal principles involved. Mfrs. BIO at 27; AG BIO at 24-25. But that once again ignores the different standards applied by the circuits for finding a hybrid restraint – the essential prerequisite to the *Midcal* analysis. Furthermore, regarding the relationship between *Midcal* and *Hoover*, while Respondents decry the absence of a string-cite in the Petition, it was in fact the Ninth Circuit that identified the confusion and the cases reflecting the prob-

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[6] That this Court has, over the past eight years, denied petitions for certiorari on similar issues likely reflected the need for at least some percolation of the issues, but is no reason to deny the current petition now that the issues have indeed percolated even since the last petition denied by this Court in 2004. *See Mariana* v. *Fisher*, 338 F.3d 189 (CA3 2003), *cert. denied*, 540 U.S. 1179 (2004). Further percolation is unnecessary given the Ninth Circuit's direct confrontation of contrary circuit decisions.

lem. App. A24. The Petition's citation, at 30-31, to the opinion below thus is more than sufficient to support the existence of a problem warranting this Court's resolution. And, as explained in the Petition, at 30, the Ninth Circuit's excessive willingness to find unilateral action subject to *Hoover*, as opposed to a hybrid restraint subject to *Midcal*, severely diminishes the scope of *Midcal* both in MSA cases and elsewhere.

3. Finally, the extension of the federalism-based *Parker* doctrine to cover an agreement among numerous States that regulates a national market in cigarettes turns federalism on its head. That Congress was asked to approve such a plan and declined – hearing testimony regarding the anticompetitive nature of the then-proposed plan – speaks loudly to the federal interests involved and infringed upon by the subsequent agreement adopted without federal approval. *Freedom Holdings I*, 357 F.3d at 229 n. 23, 230 (quoting objections from FTC Chairman Robert Pitofsky). It is thus Respondents, not Petitioner, who have it "exactly backwards," Mfrs. BIO at 28-29, regarding the application of federalism principles to this case.[7]

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[7] That plaintiff did not bring a separate Compact Clause challenge is of little moment given that such a challenge would have to demonstrate infringement upon federal interests – here the interests embodied in the antirust laws – and consequently the Compact Clause is more readily viewed as one consideration in evaluating the federalism-based *Parker* defense in the context of the primary antitrust claim itself. That the Compact Clause could have formed, but was not raised as, the basis of its own claim does not denigrate it as an independently material and relevant consideration in the antitrust context.

III. The Decision Below Improperly Expands Antitrust Immunity Contrary to the Decisions of this Court.

As the Petition explained, at 32-33, the Ninth Ciruit departed from a variety of this Court's precedents, including in its incorrect application of the more rigorous standard of review in *Rice* v. *Norman Williams Co.*, 458 U.S. 654 (1982). Regardless whether this case is viewed as a facial or an as-applied challenge, it remains true that this case is brought post-implementation, with eventual access to the facts regarding the actual operation of the MSA, not merely "abstract" speculation on how the scheme might operate in the future. 458 U.S. at 661. The Ninth Circuit thus erroneously applied the stricter *Rice* standard contrary to this Court's express rationale for that standard.

And, as also explained previously, Pet. 33-34, the Ninth Circuit was indeed unfaithful to *Midcal* and its progeny by narrowing the scope of what constitutes a hybrid restraint to the point that it would seem to exclude even the restraint in *Midcal* itself. As the Second and Third Circuits recognized and the Petition explains, Pet. 25-27, the MSA scheme as alleged indeed constitutes a hybrid restraint just as readily as the restraint in *Midcal*.

Finally, as for *Noerr-Pennington*, the Petition amply explains the error in extending *Noerr-Pennington* to the results of petitioning rather than limiting it to the petitioning activity itself. Pet. 22-25, 34. The Ninth Circuit's express refusal, App. A30 n. 11, even to consider *Parker*'s application to the claims against

the OPMs thus is inconsistent with the limited scope of *Noerr-Pennington* immunity.

CONCLUSION

For the reasons above, this Court should grant the petition for a writ of certiorari.

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